SUPREME COURT, U. S.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1967.

No. 893

PUBLIC SERVICE COMMISSION OF THE STATE OF WISCONSIN,

and

CITY OF CHICAGO, A MUNICIPAL CORPORATION OF THE STATE OF ILLINOIS,

Joint Petitioners,

vs.

FEDERAL POWER COMMISSION,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT.

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THE GUNTHORP-WARREN PRINTING COMPANY, CHICAGO 56

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CITY OF CHICAGO, A MUNICIPAL CORPORATION OF THE STATE OF ILLINOIS,

Joint Petitioners,

vs.

FEDERAL POWER COMMISSION,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT.

City of Chicago and Public Service Commission of Wisconsin ("Joint Petitioners") respectfully pray that a Writ of Certiorari issue to review the judgment of the United States Court of Appeals for the District of Columbia Circuit entered in the above-entitled case on September 8, 1967.

OPINIONS BELOW.

The opinion of the Court of Appeals, Docket Nos. 19604 and 19836, decided September 8, 1967 (Appendix A), is not yet reported. Federal Power Commission's Opinions and

Orders (456 and 456-A) in the matter entitled "*Natural Gas Pipeline Company of America,* Docket No. RP61-8" were issued March 18, 1965 and June 23, 1965 respectively (R. 5118-5130, and R. 5199-5205) and its Order granting rehearing of Opinion No. 456 (R. 5198) was issued on May 12, 1965 and its Order denying rehearing of Opinion No. 456-A (R. 5239-5241) was issued on August 6, 1965 and are reported at 33 FPC 574 (1965), 33 FPC 1277 (1965) and 34 FPC 437 (1965).

JURISDICTION.

The judgment of the Court of Appeals was entered on September 8, 1967. The Court of Appeals, on October 31, 1967, granted the Joint Petitioners' Motion for Stay of the transmittal of the opinion and the certified copy of the Court's judgment in case No. 19604 to the Federal Power Commission for a period of thirty (30) days and, in the same Order of October 31, 1967, the Court denied Natural Gas Pipeline Company of America's ("Natural") Petition for Rehearing of the Court's Opinion and judgment in case No. 19836 (Appendix B). Consequently, pursuant to 28 U. S. C. A. Section 2101 (c), the Joint Petitioners have until December 7, 1967 to file their Petition for Writ of Certiorari with the Clerk of the United States Supreme Court.[1]

The jurisdiction of this Court is invoked under the provisions of 28 U. S. C. A. 1254 (1) and Section 19 (b) of the Natural Gas Act.[2]

---

1. Act of June 25, 1948, c. 646, 62 Stat. 961; May 24, 1949, c. 139, § 106, 63 Stat. 104.

2. Act of June 21, 1938, c. 556, § 19, 52 Stat. 831, as amended 15 U. S. C. 717r (b) (1958).

QUESTIONS PRESENTED.

1. Whether the Court erred in sustaining the Federal Power Commission's action in establishing the effective date of the filing of rate schedules and refunds incident thereto as of February 3, 1964, in lieu of March 1, 1961, the date the Joint Petitioners maintain was agreed to by the parties in their Settlement Agreement of June 21, 1962 and which Settlement Agreement was approved by the Commission in Opinion No. 367 issued on October 25, 1962?

2. Whether the Court erred in sustaining the Federal Power Commission's action, which the Joint Petitioners maintain is contrary to the provisions of Section 4(e) of the Natural Gas Act, in ordering the filing of rate schedules, and refunds incident thereto, on that portion of the rates found unjust and unreasonable, to a date other than the date upon which the rates under investigation became effective?

STATUTES INVOLVED.

The relevant parts of the statutes and the amendment to the United States Constitution are set forth in Appendix C. Citations to them are:

1. Administrative Procedure Act, Act of June 11, 1946; c. 324, 60 Stat. 235, 5 U. S. C. § 1000; § 5, 5 U. S. C. § 1004; § 8 (b), 5 U. S. C. § 1007 (b).

2. Natural Gas Act of June 21, 1938, c. 556, 52 Stat. 821, as amended 15 U. S. C. § 717c; § 5, 15 U. S. C. § 717d; § 19 (b); 15 U. S. C. § 717 (r) (b).

3. Fifth (V) Amendment to the United States Constitution.

STATEMENT OF CASE.

A. Proceeding Before the Commission.

Natural Gas Pipeline Company of America (Natural) and Peoples Gulf Coast Natural Gas Pipeline Company (Peoples Gulf Coast) which was subsequently acquired by Natural on September 29, 1960 (CP 60-97), filed on August 29, 1960 Revised Tariff Sheets which would increase rates effective October 1, 1960. These filings were made under Section 4(e) of the Natural Gas Act and pursuant to said Act were suspended for five months. The increased rates went into effect on March 1, 1961 subject to refund and were duly passed on to Natural's customers. Hearings regarding these increased rates commenced on June 20, 1961.

Subsequent to the conclusion of the Hearings and the filing of its Initial Brief on February 27, 1962, Natural prepared and submitted to the parties to the proceeding, including the Commission's Staff, a Proposal for Settlement of the issues in this proceeding. Following several conferences of the parties, a Stipulation and Agreement to terminate proceedings was prepared by Natural's Attorneys and transmitted to the City's Attorney by cover letter dated May 10, 1962 which letter is set forth as Appendix D. The Stipulation and Agreement was incorporated into the record and made part thereof on June 21, 1962 (R. 4328-9). The Commission accepted and approved this Stipulation and Agreement (hereinafter referred to as "Settlement Agreement") without change by Order issued on October 25, 1962 in Opinion No. 367, set forth as Appendix E. The Settlement Agreement reserved two issues and at the same time approved an immediate refund in excess of $8,800,000.00 to jurisdictional customers

of Natural covering the period from March 1, 1961 when Natural began collecting the filed rates under bond until the date on which the Settlement Agreement became effective.

The Settlement Agreement was entered into by all parties to the proceeding except Intervenors, Fuels Research Council, Inc., United Mine Workers of America, and Mid-West Coal Producers Institute, Inc. They objected to the proposed Settlement Agreement on the ground that the rate design did not enable Natural to recover through the commodity component of its tariff all expenses classified as commodity costs. This issue was resolved by the Commission by Paragraph (B) of Opinion No. 367 (issued October 25, 1962) where it stated:

> "The Settlement of the proceeding in Docket No. RP61-8 as set forth in Natural's proposed Settlement and Agreement is hereby approved and made effective subject to the terms and conditions hereinafter ordered." (Appendix E, p. 64.)

The provisions of the Settlement Agreement which Joint Petitioners deem of critical importance in this petition is appended hereto as Appendix F.

The major issue which was reserved for determination by the Commission as stated in Opinion No. 367 was:

> ". . . whether Natural should 'normalize' its tax expense to eliminate the effect of Internal Revenue Code § 167,26 U. S. C. A. § 167, relating to accelerated depreciation, or should compute its tax expense on the basis of taxes actually paid during the test year (1960). The Settlement provides further that pending our decision on these issues, Natural shall collect revenues subject to refund based upon a 52 per cent tax rate and 'normalized' depreciation." (Appendix E, pp. 58-59.)

On May 11, 1964 (R. 4776-84) the City filed a motion to decide the reserved issue relating to accelerated depreciа-

tion. On May 19, 1964 Natural filed an answer to the City's motion. This answer contained an offer to reduce rates effective October 1, 1965, subject to certain conditions. This rate reduction proposal was unacceptable to the City of Chicago and on July 31, 1964, the Commission ordered that briefs be filed by the parties "on the matters presented by the reserved issue of proper rate treatment of liberalized depreciation under Section IV, Paragraph (2) of the Settlement Agreement in this Docket."

B. The Commission's Opinions.

After briefs and oral arguments, the Commission issued its Opinion No. 456 dated March 18, 1965, set forth as Appendix G in which the Commission:

(a) Ruled that Natural should apply flow-through principle but as of February 3, 1964 rather than Natural's proposed October 1, 1965 date or the City's and Public Service Commission of Wisconsin's date of March 1, 1961 (R. 5126).

(b) Ruled that Natural should also apply the "rate based reduction" principle as of February 3, 1964.

(c) Ruled that the refunds and rate reductions flowing from (a) and (b) need not be effectuated until 30 days after Opinion No. 417 (*Alabama-Tennessee*, case 31 FPC 208, affirmed, 359 F. 2d 318 (C. A. 5), certiorari denied, 385 U. S. 847) becomes final.

On April 16, 1965, timely Application and Petition for Rehearing and Modification of Order and Other Relief of Opinion No. 456, was filed by the City of Chicago as provided by Section 19(a) of the Natural Gas Act (15 U. S. C. § 717r) (R. 5134-63).

On April 19, 1965, the Public Service Commission of Wisconsin timely filed an application for rehearing of Opinion No. 456 by adopting the Application and Petition for Rehearing and Modification of Order and Other Relief filed by the City of Chicago (R. 5192).

On April 19, 1965, Natural filed its Petition for Rehearing of Opinion No. 456 (R. 5164-91).

On May 12, 1965, the Federal Power Commission issued an Order which granted rehearing for the purpose of further consideration of Opinion No. 456 and Order issued March 18, 1965 (R. 5198).

On June 23, 1965, the Commission issued its Opinion No. 456-A set forth as Appendix H, which slightly modified Opinion No. 456 but which still affirmed those findings of Opinion No. 456 which the Joint Petitioners sought rehearing. On July 9, 1965 Natural filed an application for rehearing of Order and Opinion No. 456-A issued on rehearing (R. 5206-23).

On July 23, 1965 the City filed an Application for rehearing of Opinion No. 456-A as provided by Section 19a of the Natural Gas Act (15 U. S. C. § 717r) (R. 5224-38). At the same time, the City filed a Petition for the issuance of a Declaratory Order to Remove an Uncertainty (R. 5233-38). This Petition of the City requested that the Commission reject all Applications for rehearing of Order and Opinion No. 456-A issued on rehearing, since it was the City's position that the Natural Gas Act and the Commission's own rules did not provide for rehearing of Orders issued on rehearing.

On August 6, 1965 the Commission issued an Order in response to the City's aforesaid Petition. The Commission's Order rejected the City's Application for rehearing of Opinion No. 456-A issued on rehearing and partially rejected and partially denied Natural's petition for rehearing of Order and Opinion No. 456-A (R. 5239-41). This rejection by the Commission of the City's Petition for rehearing of opinion and Order 456-A made the order issued on June 23, 1965 a final Order upon which the City and the Public Service Commission of Wisconsin sought

Appeal under Section 19(b) of the Natural Gas Act (15 U. S. C. 717r(b)).

C. Proceedings in the Court Below.

On August 11, 1965 at 9:00 a.m. E. D. S. T. Joint Petitioners filed with the Clerk of the United States Court of Appeals for the District of Columbia Circuit, a Petition for Review of Certain Orders of the Federal Power Commission including Order and Opinion Nos. 456 and 456-A. On August 10, 1965 Natural mailed to the Clerk of the United States Court of Appeals for the Third Circuit, a Petition for Review of Opinion and Order Nos. 456 and 456-A.

The venue question was resolved by court order and on November 9, 1965, the Clerk of the United States Court of Appeals for the District of Columbia Circuit, Nathan J. Paulson, confirmed that the Federal Power Commission had certified and filed the record in Docket No. RP61-8 (Case No. 19604) to that Court.

Upon due consideration of the briefs and oral argument, the Court, on September 8, 1967 issued its decision in cases Nos. 19604 and 19836. Judge Leventhal, speaking for the unanimous Court, affirmed the Commission's Opinions 456 and 456-A which required Natural to flow through to the consumers the Federal Income Tax benefits realized through the use of liberalized depreciation (pages 4-14). The Court reversed the Commission's deduction from Natural's rate base of previously accumulated deferred taxes on the ground that the said issue was not reserved, for determination by the Commission, in the Settlement Agreement (pages 15-20). The Court affirmed the Commission's decision to apply the flow through policy to Natural's rates as of the date of its *Alabama-Tennessee* decision, *i.e.* as of February 3, 1964 in lieu of March 1, 1961 or Oct. 1, 1965 as urged by Joint Petitioners and Natural respectively (page 20 and page 27).

Since the Court reversed the Commission action in deducting from Natural's rate base the previously accumulated deferred taxes, the Court vacated the Commission's Order and remanded the case to the Commission for further proceedings. By motion said remand was stayed.

REASON FOR GRANTING THE WRIT.

On June 21, 1962 the City of Chicago and Natural voluntarily entered into a Settlement Agreement (Section IV (2) of said Settlement Agreement-Appendix F) which the Joint Petitioners maintain was abrogated by the Federal Power Commission in Opinions 456 and 456-A, Docket No. RP61-8, and by the United States Court of Appeals for the District of Columbia Circuit in its decision of September 8, 1967, Nos. 19604 and 19836, in that both the Commission and the Court ruled that the Settlement Agreement did not preclude the Commission from ordering that Natural file reduced rates and make refunds incident thereto for the period commencing on February 3, 1964, the date of the Commission's *Alabama-Tennessee* decision.

The Joint Petitioners contend that the 1962 Settlement Agreement specifically provided for the ordering of rate reductions and refunds to March 1, 1961 on that portion of Natural's rates that were found, by the Commission, to be unjust and unreasonable. However, neither the Commission nor the Court of Appeals could find any language in the Settlement Agreement which would warrant the said contention of the Joint Petitioners. In fact, the Commission in determining the refund period for Natural's inflated rates, stated on page 6 of its Opinion 456:

> "We think the most equitable resolution of this is to put Natural on a par with *Alabama-Tennessee*. We shall therefore order refunds back to February 3, 1964." (Appendix G, p. 75.)

The Joint Petitioners contend that the Commission, under a Section 4(e) proceeding, does not have the statutory authority or power to make its order retroactive to any date which the Commission might feel is equitable to the parties, but that Section 4(e) specifically provides that the retroactivity of the Commission's Order must relate back to the date that the rate change, which was subsequently found unjust and unreasonable, became effective and was collected from the natural gas consumer. See: *United Gas Pipeline Company* v. *Mobile Gas Corporation,* 350 U. S. 332, 341 (1956).

In dealing with this issue the lower Court in this proceeding, on pages 22 and 23 of its decision, asserted:

> "It is argued to us that Section 4(e) 'does not confer equity powers' upon respondent Commission. It may readily be agreed that a commission does not have the same range as an equity court to summon powers to the call of justice. It likewise does not have the power to punish for contempt. However, when an agency is exercising powers entrusted to it by Congress, it may have recourse to equitable conceptions in striving for the reasonableness that broadly identifies the ambit of sound discretion." (Appendix A, p. 41.)

By ignoring the explicit language of the Settlement Agreement and by sanctioning the Commission's newly derived equity powers, the Court has endorsed a $34 million bonanza to Natural and thereby has deprived the natural gas consumer of their Constitutional rights under the due process clause of the Fifth (V) Amendment to the United States Constitution.

The Court and the majority of the Commission (Commissioner Black on page 1 of his dissent-Opinion 456, held that Natural should make refunds retroactive to March 1, 1961) have, by their action, placed a shadow on the Settlement Procedure which has been used as a vehicle for

avoiding protracted litigation and will have the effect of encouraging the natural gas pipeline industry to seek rate increases, even though the increases may be questionable or specious, in expectation of an "equitable resolution", identical to the instant case, and which Commissioner Black, on page 3 of his dissent in Opinion 456, aptly describes:

> "The majority justifies the result on 'equitable' grounds. The gas consumers in the Chicago area who are, in the final analysis, being compelled to bestow a windfall of more than $30 million on Natural Gas Pipeline Company of America, will surely be surprised to learn that this constitutes 'equity' in view of the Federal Power Commission." (Appendix G, pp. 82-83.)

A. The Parties Intended and the Settlement Agreement Explicitly Provides for Retroactive Refunds to March 1, 1961, Should the City's Position Be Sustained.

On March 1, 1961 Natural placed into effect increased rates pursuant to revised tariff sheets filed with the Commission on August 29, 1960. Hearings were held before a duly authorized Examiner and in order to resolve certain disputed issues which arose during the course of the proceeding, Natural's Attorney transmitted a letter dated May 10, 1962 to the Corporation Counsel of the City of Chicago to which the Settlement Agreement was attached. The City, upon consideration of the Settlement Agreement as amplified and explained by the cover letter, agreed to the Settlement.

In the third paragraph of the cover letter, Natural's Attorney stated:

> "Natural also agrees to go to trial before the FPC on two issues and if it loses on either, to make *additional refunds* and *rate reductions* (over and above the unconditional ones mentioned above). As you recall, one of these issues which will go to trial—the normaliza-

tion of taxes—is going to trial at your request" (Emphasis supplied by Natural's Attorney). (App. D, p. 55.)

A reading of this paragraph leaves no doubt in the reader's mind that the City of Chicago and Natural intended that they go on trial before the FPC on two issues (one issue being the rate treatment of liberalized depreciation) and if Natural loses on either issue, to make additional refunds which would relate back as the then imminent refunds referred to in paragraph 2, had related back to March 1, 1961.

In order to consummate this Settlement Agreement there had to be a meeting of the minds. This meeting of the minds occurred in 1962 and provided for refunds in the event of a contingency namely, if Natural was not successful in sustaining its position that normalization was the proper rate treatment for the tax benefits of liberalized depreciation for Federal income tax purposes. Clearly, the parties could not have intended that the refunds, if any, would be retroactive to 1964, as the Commission has found, since it was very possible that the entire controversy could have been decided by the Commission in 1963.

The Commission in Opinion 456 states:

"... there is no language in the Settlement Agreement which can fairly be interpreted as requesting us to order refunds retroactive to the date the rate increase was put into effect by Natural." (App. G, p. 72.)

The statement on which the Commission relies is made notwithstanding the language of the Settlement Agreement and the nature of the proceedings, since paragraph 3, Section IV(2) of the Settlement Agreement provides:

"... Natural ... shall make such further refunds with interest at 7% per annum from the 20th day of each month in which each excess payment was collected, to the date Natural refunds such excess payments." (Appendix F, p. 67.)

Since Natural has collected these excess payments resulting from the normalization of the tax benefits of liberalized depreciation since March 1, 1961, it is obvious that rate refunds must be ordered retroactive to that date. The Commission does not have the discretion to modify the Settlement Agreement without the consent of all parties.

It might be noted that the Commission's own Staff agreed that the refunds relating to the use of liberalized depreciation should relate back to March 1, 1961.

B. The Federal Power Commission Exceeded Its Power and Authority Under Section 4(e) of the Natural Gas Act.

This Court has declared as early as the *Hope Natural Gas* case, 320 U. S. 591, 610 (1944) that the primary aim of the Natural Gas Act was:

> "... to protect consumers against exploitation at the hands of Natural Gas Companies;" also *Sunray Mid-Continent Oil Company* v. *FPC*, 364 U.S. 137, 147 (1960).

This Court has also interpreted the power of the Federal Power Commission under the Natural Gas Act in protecting the consumers as follows:

> "The powers of the Commission are defined by §§ 4(e) and 5(a).... The basic power of the Commission is that given it by § 5(a).... All that § 4(e) does, however, is to add to this basic power in the case of newly changed rates or contracts.... The further powers (1) to preserve the *status quo* pending review of the new rate by suspending its operation for a limited period, and (2) thereafter, *to make its Order retroactive, by the means of the refund procedure, to the date the change became effective.*" (Emphasis supplied.) *United Gas Pipeline Company* v. *Mobile Gas Corporation*, 350 U. S. 332, 341 (1956); and *Federal Power Commission* v. *Hunt*, 376 U. S. 515, 522 (1964).

In establishing the refund period in this proceeding, the Commission on page 6 of its Opinion, stated:

> "We think the most *equitable resolution* of this is to put Natural on a par with *Alabama-Tennessee*. We shall therefore order refunds back to February 3, 1964". . . . (Emphasis supplied.)

In making the foregoing decision, the Commission ignored the fact that this was a Section 4(e) proceeding and that its powers under this section as interpreted by the Supreme Court of the United States do not include the power to make its Order under a section 4(e) proceeding retroactive to any date which the Commission might feel equitable, but specifically relates the retroactivity of the Commission's Order to the date the rate change became effective. *United Gas Pipeline Company* v. *Mobile Gas Corporation, supra.* The date on which the rates became effective in this proceeding was March 1, 1961; therefore the Federal Power Commission lacks the power or authority to make refunds effective on any other date.

Commissioner Black, in his dissent, fully agrees with the position of the City and Public Service Commission of Wisconsin that the refund should relate back to the date when the increased rates went into effect when he asserted that:

> "The Commission should order Natural to refund the excess revenues collected by reason of its 'normalized' treatment of liberalized depreciation for the entire period the inflated rates have been in effect; that is from March 1, 1961 to the present." (Appendix G, p. 79.)

The Commission asserts on page 4 of its Opinion No. 456 that:

> ". . . there is no language in the Settlement which can fairly be interpreted as requiring us to order refunds retroactive to the date the rate increase was put into effect by Natural." (R. 5128.)

This is clearly erroneous since the Settlement must be read in the setting of the Natural Gas Act. In *Texas-Eastern Transmission Corporation* v. *Federal Power Commission*, 306 F. 2d 345, 347, 348 (1962), the United States Court of Appeals for the 5th Circuit stated:

> ". . . we recognize of course, that here as in every situation of contract interpretation the Court must put itself in the position of the parties. That means that we must read the Agreement in the setting of the Natural Gas Act".

Section 4(e) of the Natural Gas Act carries out the purpose of the Natural Gas Act to protect the consumer by allowing new rates to go into effect after a five months suspension period, subject to refund of any amounts found to be excessive to the date the change became effective.

C. The Decision of the Court Below and the Opinions of the Commission Overlooked the National Importance and Significance of This Proceeding.

Natural gas has become a necessity and no longer a luxury, if for no other reason than to help abate the ever-increasing air pollution problems which confront a substantial number of large metropolitan areas within these United States. Once a consumer is committed to this form of energy, he has made a capital expenditure which will allow him little choice among competing fuels. In recent years, consumers have become cognizant of their reliance on natural gas as an economical fuel and have demanded that they be represented by their state and local governmental agency in proceedings in which the rates of natural gas are determined.

To adjust to this mounting participation by consumer interests, State and Federal Commissions and all parties appearing before them, have resorted to the use of regula-

tory agency approved Settlements. This administrative tool will become untenable, if not completely avoided should this decision be allowed to stand. As the U. S. Court of Appeals for the Fifth Circuit, in *Texas-Eastern Transmission Corporation* v. *Federal Power Commission,* 306 Fed. 2d 345 at 347, 348 (1962) asserted:

> "... Commission approved voluntary settlements are an important and desirable mechanism as the Commission undertakes the staggering burden of dealing with the ceaseless flow of the ever-more complicated problems facing an inadequate staff as a result of the celebrated 1954 *Phillips* Decision. (*Phillips Petroleum Company* v. *Wisconsin,* 347 U. S. 672 (1954).) Consequently, settlements should be encouraged not discouraged."

The Court further stated:

> "... One sure way to discourage voluntary settlements is for the Commission at the behest of one party or the other, or ubiquitous ... intervenors, to read into contracts things which are simply not expressed or not there...."

Contrary to the admonition of the Court, this is just what the Commission did. It read its prospective-looking decision in *Alabama-Tennessee* into the Settlement Agreement in this case. Such action by the Commission, which was sustained by the Court of Appeals in 19604 and 19836, is contrary to the law as expressed in the decisions of the Federal Courts.

CONCLUSION.

Joint Petitioners respectfully request the opportunity to present these questions to the Court more fully. They are important questions of public law. Their resolution will have far-reaching effect.

They are questions affecting millions of citizens and involving billions of dollars.

Joint Petitioners respectfully submit that this petition for a writ of certiorari to the United States Court of Appeals for the District of Columbia Circuit should be granted.

Respectfully submitted,

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APPENDIX A.

Mr. Mathias M. Mattern, of the bar of the Supreme Court of Illinois, pro hac vice, by special leave of court, with whom Mr. William E. Torkelson was on the brief, for petitioners in No. 19,604.

Mr. William W. Brackett, for petitioner in No. 19,836.

Mr. Peter H. Schiff, Deputy Solicitor, Federal Power Commission, with whom Messrs. Richard A. Solomon, General Counsel, Howard E. Wahrenbrock, Solicitor at the time of argument, and Abraham R. Spalter, Assistant General Counsel, Federal Power Commission, were on the brief, for respondent.

Before BURGER, TAMM and LEVENTHAL, *Circuit Judges.*

LEVENTHAL, *Circuit Judge:* This case presents a cluster of issues concerning the proper treatment, for purposes of regulation by the Federal Power Commission of the rates of natural gas pipeline companies, of the higher deductions permitted in calculation of Federal income tax by the liberalized depreciation provisions of Section 167 of the Internal Revenue Code of 1954.[1] In addition to questions of general approach there are particular issues as to the effect of a rate settlement agreement.

1. 26 U. S. C. § 167 (1964).

I. Procedural History.

The controversy before us began when rate increases were filed in 1960 by Natural Gas Pipeline Company (Natural),[2] the petitioner in No. 19836. On Natural's motion in the ensuing proceeding under Section 4(e) of the Natural Gas Act,[3] the increased rates were put into effect on March 1, 1961, after the statutory suspension period expired, subject to Natural's obligation to make such refunds as the Commission might validly order. After a full hearing was had, but before briefs were submitted to the examiner, Natural, its customers, the City of Chicago (Chicago) and Wisconsin Public Service Commission (Wisconsin), and the Commission staff, agreed upon a rate settlement. The customers agreed to accept an increase in rates yielding approximately $6,200,000 per annum, about half the increase Natural had proposed, and Natural agreed to refund amounts already collected above the agreed-upon increase.

The settlement left open two questions for future determination, one of which relates to liberalized depreciation, and Natural agreed to abide by a Commission refund order "if any" with regard to the reserved issue, subject to its right to judicial review. On October 25, 1962, the Commission approved this settlement.[4]

On February 3, 1964, the Commission issued Opinion 417, *Alabama-Tennessee Natural Gas Co.*, wherein it announced principles concerning rate treatment of liberalized depreciation, and the City of Chicago then moved the Commis-

2. For present purposes "Natural" also includes Peoples Gulf Coast Natural Gas Pipeline Co., which filed separate rate increases but was thereafter combined with Natural.

3. 15 U. S. C. § 717c(e) (1964).

4. Opinion No. 367, 28 F. P. C. 731.

5. 31 F. P. C. 208.

sion to decide the liberalized depreciation issue with respect to Natural. On March 18, 1965, the Commission issued its Opinion 456,[6] concluding that the principles of *Alabama-Tennessee* were applicable to Natural and making certain other rulings with respect to effective date and settlement agreements that will be discussed in due course.

Petitions for rehearing were filed and denied and petitions for review under Section 19(b) of the Natural Gas Act[7] were filed both by Chicago and Wisconsin as joint petitioners in No. 19604, and by Natural in No. 19836.

Consideration by this court was deferred pending judicial review of the Commission's *Alabama-Tennessee* decision. That decision was affirmed by the Fifth Circuit in *Alabama-Tennessee Natural Gas Co.* v. *FPC,* 359 F. 2d 318 (1966). The Supreme Court denied certiorari, 385 U. S. 847 (1966).

II. The Validity of the Commission's Requirement for "Flow Through" to Consumers of the Tax Reductions Achieved by Natural Through Use of Liberalized Depreciation.

1. The Federal Power Commission, with judicial approval, has been engaged under the Natural Gas Act in regulating the maximum rates of natural gas pipeline companies by permitting rates that will yield operating revenues sufficient to cover "cost of service," a term that in essence includes, in addition to operating costs, depreciation, etc., the "return" to the company which the Commission calculates by providing a fair rate of return on a rate base equal to the amount prudently invested in utility property, and the "expense" of Federal income tax pay-

6. 33 F. P. C. 574. The petitions for rehearing were denied in Opinion 456-A, June 23, 1965, 33 F. P. C. 1277.

7. 15 U. S. C. § 717r(b) (1964).

able on the allowed return.[8]. The objective is to allow a fair profit, after taxes, ascertained after taking into account "a variety of factors, such as the risks of the business, the necessity for attracting capital, and the desirability of lower cost of gas to the public."[9]

2. Focusing on the income tax element this is regarded by regulatory commissions as part of the "cost" of service, a terminoligy in line with the general thinking of businessmen, although for various purposes economists and accountants draw a distinction between tax burden and cost. The difference is largely one of nomenclature since in any event it is necessary to provide, obtain or permit revenues after taxes that are sufficient to cover all costs other than taxes.

The general rule followed by the Commission, and indeed most if not all regulatory commission, is that the "consumers should be charged for only the actual liability for Federal income taxes."[10] However, as the Commission pointed out, in some cases normalization of tax deferrals is required lest future consumers be compelled to subsidize present consumers being served by the operations accruing tax liabilities. The specific question of the proper regulatory treatment of the liberalized depreciation tax deduction is one on which the regulatory commissions are nearly equally divided.

A bare majority use the so-called "normalization" method by which the tax expense component of cost of serv-

8. See *FPC* v. *Hope Natural Gas Co.*, 320 U. S. 591 (1944); J. BonBright, Principles of Public Utility Rates 147-283 (1961); Francis, Rate Regulation of Natural Gas Companies by the Federal Power Commission, 19 Law & Contemp. Prob. 413, 417-33 (1954).

9. *City of Detroit* v. *FPC*, 97 U. S. App. D. C. 260, 263, 230 F. 2d 810, 813 (1955). See Leventhal, Vitality of the Comparable Earnings Standard for Regulation of Utilities in a Growth Economy, 74 Yale L. J. 989 (1965).

10. *United Fuel Gas Co.*, 12 F. P. C. 251, 265 (1953).

ice is calculated by using the higher income tax that would have been payable if depreciation were calculated on the "straight-line" method almost universally utilized for tax purposes prior to the 1954 Code, without reduction for the amount of "deferred" taxes carried in a tax reserve on the books in contemplation of the future tax obligation. This approach focuses on the current tax reduction achieved by the utility as a tax "deferral," with liberalized deduction providing higher depreciation deductions and hence lower taxes in the early part of the property's usable life, and of the lower deductions and higher taxes in later years.

The rejection of the normalization approach by respondent Commission, and others, rests on the view that the deferral conception is inappropriate in the absence of a reasonably foreseeable decline in depreciable plant account, and hence is inapplicable where a growing or stable plant is ascertainable for the foreseeable future. In *Alabama-Tennessee* the Commission determined that the deferral conception was inapplicable in view of the factual condition of growing or stable plant for the foreseeable future, a condition found to exist in general for the natural gas industry and natural gas pipeline companies. The finding of this condition followed a review of forecasts for energy supply and demand and other pertinent economic data, a forecast of continuous growth characteristics for the industry for some time, albeit at a more modest rate than the dramatically steep incline that has marked the industry in the post-war decades, and a relative assurance of at least stable plant for the foreseeable future.

In *Alabama-Tennessee* the Commission rejected normalization for the natural gas industry in general, but left open the possibility that a different ruling might be applicable to a particular company that showed its condition was different from the industry's in this regard. No such showing was attempted by Natural, and there is no serious

effort in this case to dispute the factual finding underlying the flow-through determination, similar to that made for the company in *Alabama-Tennessee,* that "Natural will maintain a growing or stable plant for the foreseeable future."

3. We follow the decision of the Fifth Circuit in *Alabama-Tennessee* which sustained the Commission's findings as reasonable and supported by evidence and upheld the general validity and particular application of the policy determination requiring "flow-through" of the tax reduction ascribable to liberalized depreciation. Although in general the denial of certiorari is said to import no conclusion on the merits, it is not insignificant that in *Alabama-Tennessee* the writ was denied notwithstanding the concession of the Solicitor General that an important recurring question was involved.

In any event, *Alabama-Tennessee* is plainly in line with the principles expressed in *FPC* v. *United Gas Pipe Line Co.,* 386 U. S. 237 (1967). In that case the Court held that where affiliated companies obtain a tax saving through consolidated returns, a regulatory commission can flow through the amount it calculates, by a reasonable allocation, to be the tax saving of a regulated company within the affiliated group. The Court pointed out that the tax law does not attempt to set rates, and stated (at 244-45):

> [W]hen the out-of-pocket tax cost of the regulated affiliate is reduced, there is an immediate confrontation with the ratemaking principle that limits cost of service to expenses actually incurred. Nothing in *Colorado Interstate* or *Panhandle* forbids the Commission to recognize the actual tax saving impact of a private election to file consolidated returns. On the contrary, both cases support the power and duty of the Commission to limit cost of service to real expenses. [Footnote omitted.]

While Natural's contentions to this court are for the most part disposed of by the court's decision in *Alabama-Tennessee*, some supplementary comments may be appropriate. First, we note that it is in the tradition of sound regulation for a commission to develop doctrines, as respondent Commission has done, that are attuned to its growth forecast.[11] Indeed, it is this factual experience of renewal of capital investment that has undercut the objections of theory, once expressed by natural gas companies, that the Commission's use of prudent rate base and deduction of depreciation reserves would lead in time to the absurdity of a "vanishing rate base" and zero return.[12] Similarly here the factual projection of capital investment undercuts the objection grounded on the theoretical point that the flow-through approach exposes a company to the risk of a future tax bill without the comfort of a tax reserve.

Given the premise of a growing or stable plant, there is no basis for our rejecting as arbitrary the Commission's conclusion that the utility will obtain a continuing tax reduction from liberalized depreciation. That proposition, noted in publication,[13] and presented in this record, as in the *Alabama-Tennessee* record, through the testimony of Mr. Melwood Van Scoyoc, as a witness for intervenors, is essentially demonstrable as a matter of mathematics. The critical point is that whereas tax "deferral" is the correct analysis when only a single unit of property is involved, when the procedure is applied to "property comprised of

11. See generally Leventhal, *supra* note 9.

12. See Francis, *supra* note 8, at 425-30.

13. National Association of Railroad and Utilities Commissioners [NARUC], Proceedings, 67th Annual Convention, 1955, 439-40 (1956); Eisner, Depreciation Under the New Tax Law, 33 Harv. Bus. Rev. No. 1, 66-74 (1955); Davidson, Accelerated Depreciation and the Allocation of Income Taxes, 33 Accounting Rev. 173 (1958).

a large number of units as is characteristic of utility plant,"[14] typically with different vintages, depreciated through use of "average service life" experience, composite depreciation on total plant will exceed straight line composite depreciation as long as total dollar amount of gross composite plant (before depreciation) remains at least stable, since the depreciation on older assets that is below normal "is counterbalanced by 'above normal' depreciation on new assets."[15]

Natural's primary emphasis is on the legislative intention it gleans from the tax statute. What Congress provides in a tax statute does not necessarily control in the implementation of federal regulatory statutes. *See FPC* v. *United Gas Pipe Line Co., supra.* In *Alabama-Tennessee*, after reviewing the legislative history at length, after contrasting the Congressional silence on the liberalized depreciation issue with the precise language used in the provision of the tax statute that expressly restricted the rate-making authority of federal regulatory agencies to reduce the federal income tax component of cost of service by the amount of the investment tax credit,[16] and after projecting as well as it could how the legislature would have dealt with the concrete situation if it had but spoken,[17] the Fifth Circuit concluded (359 F. 2d at 335):

> Given the long reach of the Natural Gas Act, as liberally interpreted by the Supreme Court, and weighing the consumer-oriented objectives of that Act against

14. 1955 NARUC Proceedings, *supra* note 13.

15. See *Alabama-Tennessee Natural Gas Co.* v. *FPC*, *supra*, 359 F. 2d at 336.

16. See *North Central Airlines, Inc.* v. *CAB*, 124 U. S. App. D. C. ...., 363 F. 2d 983 (1966).

17. Judge Learned Hand in *United States* v. *Klinger*, 199 F. 2d 645, 648 (2d Cir. 1952): "Flinch as we may, what we do, and must do, is to protect ourselves, as best we can, into the position of those who uttered the words, and to impute to them how they would have dealt with the concrete occasion."

> the Section 167 objective of promoting plan expansion by postponing the timing of tax payments, we conclude: It is unlikely to suppose that Congress amended the Natural Gas Act by a reference in the Internal Revenue Code; it is unreasonable to read Section 167 as a mandate reducing the Commission's responsibility to fix fair rates according to its usual ratemaking policies in favor of the consumer. * * * [We] infer that its [Congress'] decision not to disturb, in terms, the status quo of ratemaking indicates a congressional intent that each federal regulatory agency should continue to exercise an informed discretionary authority in accordance with the agency's usual standards in the light of the needs peculiar to the particular industry subject to rate regulation.

The fact that the tax statute is not controlling does not necessarily end the matter. A regulatory agency may, should, and in some instances must, give consideration to objectives expressed by Congress in other legislation,[18] assuming they can be related to the objectives of the statute administered by the agency.[19] Here, however, the Commission did give consideration to the Congressional objective of stimulating investment. It pointed out that the major expenditures by natural gas pipelines result from system expansion to serve additional loads, and technological obsolescence has not been a large investment factor; that lower rates tend to generate higher volume and thus ultimately to require expansion; that natural gas pipelines have no need for the additional capital provided by tax reserves to finance expansion in view of the regulatory principles under which rate of return is established so as to attract new capital and there is provision for adequate working capital allowance in the rate base; and that there

18. *California* v. *FPC*, 369 U. S. 482 (1962); *City of Pittsburgh* v. *FPC*, 99 U. S. App. D. C. 113, 126, 237 F. 2d 741, 754 (1956).

19. *American Overseas Airlines* v. *CAB*, 103 U. S. App. D. C. 41, 254 F. 2d 744 (1958).

is no indication that pipelines will have any problem financing the moderate expansion expected in the near future, especially in view of the tremendous expansion financed in the past two decades at a cost of over $9 billion. The Commission applied to Natural its rationale in *Alabama-Tennessee* "that flow-through and lower rates are a more effective stimulus to new investment than normalization"; and Natural does not contend that if it be assumed that the approach is sound for the natural gas pipeline industry generally it is not properly applicable to Natural.[20]

Natural's position is that the Commission is required not only to further the Congressional objective of enhancing investment, but to adopt the method prescribed by Congress for achieving that objective, and that Congress sought economic stimulus through the technique of providing current investment funds and not through the technique of tax reduction. We do not read the legislative history as indicating that Congress would have felt frustrated if producers in a competitive industry decided to treat the liberalized depreciation as in effect a tax reduction and to lower prices in contemplation of increasing sales and capital investment. The regulation of companies protected from free competition may properly be conducted so as to seek the kind of service and price reductions that would have been achieved under free competition—assuming the utility

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20. The Commission found: "Natural is an expanding enterprise, and will continue to expand in the foreseeable future. Natural apparently does not dispute the fact that it is properly subject to the principles enunciated in *Alabama-Tennessee* if that case is upheld."

While the Commission's earlier findings that *Alabama-Tennessee* was favorably situated in regard to raising of capital were not specifically repeated for Natural, the fact is not contested by Natural. *Cf. FPC* v. *Natural Gas Pipeline Co.*, 315 U. S. 575, 597 (1942).

is not deprived of a fair return.[21] In any event, we agree with the conclusion of the Fifth Circuit that the courts are not in a position to choose between economic theories or to mandate the particular technique espoused by Natural as the plainly ascertainable will of Congress.

4. Natural says that the Commission has been treating the courts as "rubber stamps," stating in its brief: "It has repeatedly changed its position and each time it has ignored prior judicial holdings, apparently confident that it will be upheld in its new-found reversible exercise of 'expertise.' If the Commission can successfully do this—if its decisions can be relied upon only until the composition of the Commission changes and a different social philosophy gains control—and can secure judicial approval each time it switches position, then Natural submits that judicial review has lost its meaning."

In reply, respondent's brief retraces the Commission's steps and argues that they were responsive to growing appreciation of the consequences of the normalization approach and to new judicial indications of the range of discretion available to the Commission. Natural disputes the reading of pertinent decisions both by the Commission and in the *Alabama-Tennessee* decision of the Fifth Circuit. So far as our own decisions go, it may be observed that in 1955

21. Compare National Association of Railroad and Utility Commissioners, Proceedings, 53d Annual Convention, 1941, 369 (1942):

> The purpose of regulatory procedure, in the protection which it is designed to afford the consumer, is to simulate and substitute the effects of competition and give the consumer the benefits which he would derive from a system of competition.

For statements in judicial decisions that "regulation takes the place of and stands for competition," see *e.g.*, *State ex rel. Kansas City* v. *Kansas City Gas Co.*, 254 Mo. 515, 534, 163 S. W. 854, 858 (1913); *State Pub. Util. Comm'n ex rel. City of Springfield* v. *Springfield Gas & Elec. Co.*, 291 Ill. 209, 218, 125 N. E. 891, 896 (1919).

City of Detroit v. *Federal Power Commission*,[22] upheld, as the result intended by Congress, the Commission's normalization approach to the accelerated amortization applicable under the 1950 Code to particular national defense facilities. The Commission's 1956 *Amere* decision[23] assumed that *City of Detroit* governed liberalized depreciation, notwithstanding the fact that the accelerated amortization provisions were concerned with particular units of plant, and did not involve the entirety of new plant covered by liberalized depreciation, which assures and generalizes the savings effect related above.

Our 1963 en banc decision in *Panhandle Eastern Pipe Line Co.* v. *Federal Power Commission*,[24] limited the scope of this part of *City of Detroit* when the court approved the 1961 determination of the Commission, faced with the mounting accumulations of tax deferrals under the normalization policy, that limited the rate of return on this part of rate base to only 1.5%. The indications of agency discretion in the majority opinion[25] were relied upon by the Commission as a recognition of its authority when it

22. 97 U. S. App. D. C. 260, 230 F. 2d 810, cert. denied, 352 U. S. 829, rehearing denied, 352 U. S. 919 (1956).

23. *Amere Gas Util. Co.*, 15 F. P. C. 760, 781, petition for review dismissed, 16 F. P. C. 880 (1956). *City of Lexington* v. *FPC*, No. 13590 (June 26, 1957) (unreported).

24. 115 U. S. App. D. C. 8, 316 F. 2d 659, cert. denied, 375 U. S. 881 (1963).

25. The dissenting opinion was based on the premise that liberalized depreciation works a deferral of taxes, and that the Commission's switch in position between *Phillips Petroleum Co.*, 24 F. P. C. 537, and *Northern Natural Gas Co.*, 25 F. P. C. 431, was in "defiance" of our *City of Detroit* opinion. The majority opinion stated that nothing in the language or legislative history of Section 167 "indicates that Congress considered its regulatory consequences," characterized as merely "arguable" the possibility that regulatory decisions would be governed by the tax purpose of Congress, and held that even so that purpose was not thwarted by an action that retained some incentive to investment, and found the Commission had not abused its discretion.

acted within a year to reject completely the "normalization" approach.

The Rule of Law does not forbid an agency from modifying its regulatory policy, and the courts have upheld policy revision many times.[26] Indeed one of the signal attributes of the administrative process is flexibility in reconsidering and reforming of policy. What is required by the Rule of Law is that agency policies and standards, whether or not modifications of previous policies, be reasonable and non-discriminatory, and flow rationally from findings that are reasonable inferences from substantial evidence.

There is perhaps one additional requirement inserted in case of a change in policy, that the agency give due consideration to the equities, if any, arising out of commitments based on previous rulings.[27]

The possibility that changes in policy and viewpoint may come with changes in membership is inherent in an agency's characteristic as an institution headed and staffed by human beings, and will not come as a surprise to any observed of the administrative process.[28] Sometimes indeed an industry resists renomination of a commissioner precisely to obtain a change in policy. It is not necessarily invidious that a change in approach may reflect a change in personnel; indeed, it may well be a blessing rather than a vice that the rigidity of staff bureaucracy may be mini-

26. *New Castle County Airport Comm'n* v. *CAB*, ... U. S. App. D. C. ...., 371 F. 2d 733 (1966), cert. denied, 387 U. S. 930 (1967); *Philadelphia Television Broadcasting Co.* v. *FCC*, 123 U. S. App. D. C. 298, 359 F. 2d 282 (1966). As Judge Prettyman said in *Pinellas Broadcasting Co.* v. *FCC*, 97 U. S. App. D. C. 236, 238, 230 F. 2d 204, 206, cert. denied, 350 U. S. 1007 (1956): "[T]he Commission's view of what is best in the public interest may change from time to time. Commissions themselves change, underlying philosophies differ, and experience often dictates changes." (Emphasis added.)

27. See, *e.g.*, *NLRB* v. *International Bhd. of Teamsters*, 225 F. 2d 343, 348 (8th Cir. 1955).

mized by changes of agency membership that can initiate a fresh look at old problems, rather than a mechanical perpetuation of what has been done in the past. In any event, judicial review is not abdicated by a doctrine that accepts an agency discretion to change policies, but rejects rulings based on improper pressures on or even secret contacts with administrators,[29] the exercise of pure whim, or other irrational or arbitrary bases of decision.

Insofar as Natural relies on the inaction of Congress during the years of the Commission's normalization rulings, this does not significantly add to or subtract from the legislation as passed in 1954. Sometimes legislative inaction may be taken as acquiescence in the validity of executive or administrative action under an assumed power.[30] More rarely can it be taken as a prohibition where there has been executive inaction or delay in apprehending the scope and nature of the evil that is later considered to require attention in the public interest.[31]

We affirm the Commission's policy use of the "flow through" of the current tax reduction resulting from use

28. *Braniff Airways, Inc.* v. *CAB*, ... U. S. App. D. C. ...., ... F. 2d .... (No. 20160, April 12, 1967); see also *NLRB* v. *International Bhd. of Teamsters, supra* note 27.

29. *WKAT, Inc.* v. *FCC*, 111 U. S. App. D. C. 253, 260-61, 296 F. 2d 375, 382-83, cert. denied sub nom. *Public Service Television, Inc.* v. *FCC*, 368 U. S. 841 (1961).

30. *Massachusetts Trustees of E. Gas & Fuel Associates* v. *United States*, 377 U. S. 235, 241 (1964); *Power Reactor Dev. Co.* v. *International Union of Elec. Workers*, 367 U. S. 396, 409 (1961) (but cautions it "may often be shaky business to attribute significance to the inaction of Congress"); *United States* v. *Shreveport Grain & Elevator Co.*, 287 U. S. 77, 84 (1932).

The foregoing doctrine on inference of legislative acquiescence is over and beyond the general doctrine of deference to an administrative interpretation, see *Udall* v. *Tallman*, 380 U. S. 1, 16 (1965).

31. *United States* v. *Morton Salt Co.*, 338 U. S. 632, 647-48 (1950) (powers "are not lost by being allowed to lie dormant"); cf. *Buckeye Cablevision, Inc.* v. *FCC*, ... U. S. App. D. C. ...., ... F. 2d .... (No. 20274, June 30, 1967).

of liberalized depreciation and its application of that policy in limitation of Natural's rate increase.

III. Invalidity Under Settlement Agreement of the Commission's Deduction from Natural's Rate Base of Previously Accumulated Deferred Taxes.

The Commission, after concluding that Natural's condition was properly governed by the principles of *Alabama-Tennessee,* decided that as was done in that case "we shall provide for deduction of the accumulated reserves from the rate base." We think this action was precluded by its 1962 order approving the parties' Stipulation and Agreement to Terminate Proceedings, hereafter referred to as their Settlement Agreement.

In *Alabama-Tennessee,* after adopting the flow-through policy, the Commission turned to the existing accumulation of deferred tax reserves, and held they should be maintained as contingency reserves against the remote possibility that due to some improbable but conceivable combination of circumstances future ratepayers may be called upon to defray the cost of higher taxes attributable to the earlier use of liberalized depreciation. It concluded that since the accumulations will not be needed in the foreseeable future to defray any increase in taxes payable on earnings from properties used in rendering service, the balances "must now be regarded as consumer-contributed capital collected for a specific purpose of remote and improbable occurrence."[32]

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32. 31 F. P. C. at 220. The Commission instituted a rule-making procedure to conform accounting regulations for recording tax balances to this determination.

The funds in Account 282 had previously been restricted against distribution in dividends, the Commission having specifically found they should be added to supply part of the capital requirements. *Northern Natural Gas Co.,* 25 F. P. C. 431, 438, 441 (1961). They were thus different in kind from general revenues received without restriction as to disposition, cf. *El Paso Natural Gas Co.* v. *FPC,* 281 F. 2d 567, 573-74 (5th Cir. 1960).

The Commission formulated the policy, prospective in effect from the date of the order, that the rate of return on these balances should be zero, since no cost had been incurred in their accumulation, and it accordingly modified its policy of permitting gas pipeline companies to earn a 1.5% return on those balances.[33]

As to the general propriety of such an approach, assuming a flow-through policy, we agree with the Fifth Circuit's affirmance of this ruling in *Alabama-Tennessee*. We agree with Natural, however, that the Commission's application of this ruling to Natural was in excess of the question reserved for the Commission by the Settlement Agreement, which uses explicit and unambiguous language reserving only the question whether Natural should use "flow through" or "normalization" in computing its federal income tax expense allowance.[34] Opinion No. 367 approving

33. The previous policy of 1.5% rate of return on these balances was the determination affirmed by this court in *Panhandle E. Pipe Line Co.* v. *FPC*, *supra* note 22.

34. Section IV(2) of the Settlement Agreement provides:

"2. The question of whether Natural, in computing its cost of service for rate purposes, should compute its federal income tax expense allowance by 'normalizing' such taxes to eliminate the effect of Section 167 of the Federal Internal Revenue Code, which relates to 'accelerated' or 'liberalized' depreciation, or by utilizing the principle of 'flow through' of the tax effect of the use of such 'accelerated depreciation' deductions for tax purposes, as proposed and defined by the City of Chicago in these proceedings, rather than the 'normalization' method, shall be determined by an adjudication by the Commission in these proceedings and this issue shall not be terminated by approval of the settlement proposed hereunder.

* * * * *

"In the event it shall be determined in these proceedings by a valid and final order of the Commission that Natural, in computing its cost of service in these proceedings, must utilize the above mentioned 'flow through' method of tax computation, Natural, subject to its right to seek judicial review thereof, shall make such further refunds, with interest at 7 per cent per annum from the 20th day of each month in which each excess payment was collected, to the date Natural refunds

the Settlement Agreement uses the same terminology, and makes no reference to other aspects of liberalized depreciation problem, such as effect on rate base or rate of return. Any adjustment in rate base or rate of return would affect the "return" component of the cost of service which is separate and distinct from the Federal Income Tax expense allowance. The difference between these two items is not recondite technicality; it is part of the basic vocabulary of all parties and counsel to a rate proceeding.[35]

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such excess payment, as shall result from the reduction, if any, in the level of any of the rates contained in its FPC Rate Schedules that may be required by the Commission at the time of such order; provided, however, that Natural's obligation to make a refund hereunder shall not become effective unless and until the aggregate sum refundable under this Paragraph (2) shall be equal to $100,000.

"It is agreed that the difference between the depreciation deduction used in computing the Federal Income Tax allowance by use of the above mentioned 'normalization' method, which is included in the cost of service of $137,014,823, and the depreciation deduction for such tax allowance purposes, relative to such cost of service, which would have resulted from use of the above mentioned 'flow through method' is $7,928,320. Any refunds and/or rate reductions made by reason of this Section IV(2) shall be made as described in the last paragraph of Section IV(1) above."

35. The Commission brief concedes that "the return allowance itself, as opposed to the consequent tax allowance, is not within the literal language of the settlement."

No element of "return" is inserted by the provision of the settlement that the Commission shall decide whether to compute federal income tax expense allowance by utilizing the "flow through" principle of the tax effect "as proposed and defined by the City of Chicago in these proceedings, rather than the 'normalization' method."

Mr. Van Scoyoc's prepared testimony and exhibits, with computations of tax impact, nowhere refer to the "return" problem. After he noted that the Company's cost of service exhibit ignored the $8,124,909 shown in the Staff exhibit as tax deductions due to liberalized depreciation, Mr. Van Scoyoc was asked: "Q. If the principle of actual taxes were used in the Company's cost of service as you advocate what would be the effect on the ratepayer of utilizing this $8,124,909 in available tax deductions in computing income taxes for cost of service purposes?

"A. It would result in lowering the cost of service by 108⅓

In denying Natural's petition for rehearing the respondent Commission said that the determination of the issue whether Natural was properly subject to flow through "also involved, in our opinion, the proper treatment of the accumulated deferred taxes," since these reserves reflect the benefits of depreciation that had not been flowed through. We have no doubt that the two subjects are inter-related, as the discussion in *Alabama-Tennessee* makes clear, but we also have no doubt that they are two separate subjects, and that under the Settlement Agreement one was settled by the parties and one was reserved for Commission decision.

The case is governed by the need for construing settlement agreements in accordance with the specialized understanding of parties to a rate proceeding. There is little we can add to the Fifth Circuit's knowledgeable discussion of settlement agreements and their interpretation in *Texas Eastern Transmission Corp.* v. *FPC*, 306 F. 2d 345 (1962) at 348:

> • • • [O]ne sure way to discourage voluntary settlements is for the Commission, at the behest of one party or the other, or the ubiquitous intervenors, to read into contracts things which are simply not expressed or not there, out of the thoroughly commendable (and understandable) feeling that unless that is done the result is not as good as it ought to have been. This is particularly true in this area where, as was the case here, the proposed settlement is subjected, as it should be, to the closest scrutiny by the Commission and its staff. It is more than arms' length. Overreaching is

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percent of $8,124,909 or $8,801,982, assuming the use of a 52 percent tax rate.'"

Mr. Van Scoyoc's response shows the effect of a different tax allowance without any adjustment of the return component. His statement on cross-examination cited in the Commission's brief states what he thinks return should be (zero), but does not state that this is the same as the issue of the determination of the tax expense allowance.

an impossibility. But precision is not merely a possibility. Precision is almost a certainty as skilled partisans undertake to hammer out the bargain under the ever-present watchful eye (and hand) of the independent agency as the guardian of the public interest. Consequently, both in its substantive provisions and in the terminology sought to memorialize the undertaking, the parties ought to be able to accept the contract as drafted, executed and approved. It should stand for what it says.

In construing the contract in accordance with its terms, and incidentally in a way that Chicago as well as Natural tells us is sound, we observe that this is not necessarily the perpetuation of an unintended and egregious mistake. We note that Mr. W. H. Beidatsch, the Commission staff witness, calculated that fair rate of return, was 6.28%, if the "capital obtained through the deferral of income taxes" is assumed to be "cost free", and 6.32% if a cost of 1.5% "is imputed to such capital." So the parties and staff were not unaware of the problem. And the City of Chicago in particular was presumably not unaware that only two years previously the Supreme Court of Illinois held that the state commission could in its discretion recognize deferred tax liability as a present expense, but could not fail to exclude from rate base the funds generated by accruing deferred tax expense.[36]

The Settlement Agreement says the agreement by the parties as to amount of cost of service, reached for purposes of settlement, "is not intended to reflect agreement to the amount, percentage or method or derivation of any particular item of such cost of service." It also expressly provides that it is without prejudice to the right of the parties hereafter to question in any other proceeding the propriety of any method or principle employed or the accuracy of any

36. *City of Alton* v. *Commerce Comm'n*, 19 Ill. 2d 76, 165 N. E. 2d 513 (1960).

data used in connection with this settlement." These are important provisions. The parties may be disposed to avoid the expense and distractions of litigation if the various rates reached in a settlement do not constitute a binding admission or ruling on principle. But for purposes of considering whether it makes sense to construe the Settlement Agreement as written, it may be supposed that at least the intervenors and staff may have been satisfied that in their calculation the settlement was acceptable in that it essentially reflected a 1.5% rate of return for that part of capital composed of deferred tax accruals. Although this was no more than would have been required by the Commission's policy at the time, that policy was of only one year's standing, there was at least some question of its validity under the *City of Detroit* case, and it had not yet been affirmed by the 5-4 en banc decision which was issued by this court in 1963.[37] An agreement by Natural not to seek a greater return and by the customers and staff not to press for a zero return has every element of a meaningful bargain. That agreement was not articulated in express terms, but it is, we think, the meaning and consequence of the Settlement Agreement executed by the parties and duly approved by the Commission.

IV. Validity of the Commission's Decision to Apply the Flow Through Policy to Natural's Rates as of the Date of Its Alabama-Tennessee Decision.

The Commission concluded that the flow-through policy should be applied to Natural's rates as of February 3, 1965, the date from which the Commission decided in *Alabama-Tennessee* that tax benefits from liberalized depreciation should be flowed through. We hold the Commission's action valid, and shall state our reasons while discussing and rejecting the attacks from both sides.

37. See *Panhandle E. Pipe Line Co.* v. *FPC*, *supra* note 22.

A. Contentions of Invalidity Under the Natural Gas Act.

Chicago contends that Section 4(e) of the Natural Gas Act required the Commission to make its order retroactive to the effective date of the increased rates held invalid. Section 4(e) does give the Commission "power . . . . to make its order retroactive, by means of the refund procedure, to the date the change became effective." *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*, 350 U. S. 332, 341 (1956). That does not mean Section 4(e) requires this retroactive result. Explaining why its ruling was not made retroactive to the effective date of Natural's rate increase, the Commission stated "that in *Alabama-Tennessee* we were announcing a new policy and overruling previous decisions. It was therefore not equitable, contrary to the contentions of Chicago, to make our determination effective before February 3, 1964, but on that date the industry was informed of the new policy, and it was appropriate that refunds should be ordered from then."

Natural on the other hand contends that the Commission erred in applying its policies to Natural retroactively, that is prior to the date on which it found such policies valid as to Natural (March 18, 1965).

We reject both sets of contentions. The Commission acted sensibly and reasonably in making its new policy effective as of the date it was announced to the industry. We have recently upheld as reasonable, against a charge that retroactive application was unlawful, the Commission's determination under the Federal Power Act to make a license requirement effective as of the date it issued decisions setting forth new criteria for requirement of licenses. *Niagara Mohawk Power Corp.* v. *FPC*, ... U. S. App. D. C. ....., ... F. 2d ..... (No. 19887, May 18, 1967).

Instructive analogy is afforded by precedents of both legislative and judicial branches. Customarily decisions

of the judicial branch are retroactive and the legal principles announced by the court are considered to be the rules that governed transactions and events prior to the date of decision. But this is not a necessary feature even of the judicial process. In recent years the Supreme Court has deemed it appropriate to make several doctrines effective prospectively as of the date of its announcement of a change in the course of decision.[38] The Court has rejected the Blackstonian concept that decisions are only the exposition of pre-existing principles that are "discovered" by the "living oracle of the law," and that overruled decisions reflect only a human error in the Court failure of true discovery. Instead it took the view that even courts do more than discover the law, that overruled decisions are judicial facts and that practical consequences, such as hardship or injustice, can be taken into account in deciding whether changes in decision should be retroactive.

A similar destination is often reached from another direction by the legislative branch which customarily operates prospectively but frequently finds that the public interest lies in making legislation retroactive to the date of public awareness of consideration being given to proposed changes.[39]

The good sense and reasonableness, and hence presump-

38. *Stovall* v. *Denno*, 87 S. Ct. 1967 (1967); *Johnson* v. *New Jersey*, 384 U. S. 719 (1966); *Tehan* v. *Shott*, 382 U. S. 406 (1966); *Linkletter* v. *Walker*, 381 U. S. 618 (1965). The foregoing involve constitutional questions. However, in *James* v. *United States*, 366 U. S. 213 (1961), the Court overruled an earlier decision on a question of statutory construction (that embezzled funds are not taxable income), but declined to apply the new decision retroactively so far as criminal prosecutions are concerned. That a state court may validly limit to prospective application its reversal of view as to the meaning and application of a statute was stated in *Great Northern Ry. Co.* v. *Sunburst Oil & Ref. Co.*, 287 U. S. 358 (1932).

39. *Welch* v. *Henry*, 305 U. S. 134 (1938); *United States* v. *Hudson*, 299 U. S. 498 (1937); *Sidney* v. *Commissioner of Internal Revenue*, 273 F. 2d 928, 932 (2d Cir. 1960).

tive validity, of a determination to start the effectiveness of a new policy with the date of a public awareness, are not to be gainsaid for an administrative agency because it states, as respondent Commission did, that this solution is "the most equitable resolution" it could reach.[40] It is argued to us that Section 4(e) "does not confer equity powers" upon respondent Commission. It may readily be agreed that a commission does not have the same range as an equity court to summon powers to the call of justice. It likewise does not have the power to punish for contempt. However, when an agency is exercising powers entrusted to it by Congress, it may have recourse to equitable conceptions in striving for the reasonableness that broadly identifies the ambit of sound discretion. Conceptions of equity are not a special province of the courts but may properly be invoked by administrative agencies seeking to achieve "the necessity of control in an increasingly complex society without sacrifice of fundamental principles of fairness and justice."[41]

Upholding the Commission's action is not equivalent, as Chicago suggests, to a ruling that the agency would be free to permit the utility to retain some rates the Commission had found unjust. The point is, rather, as respondent's brief puts it, that the "Commission's decision in effect means that until February 3, 1964, the date of the *Alabama-Tennessee* decision, rates reflecting normalization were just and reasonable," while rates reflecting normalization subsequent to the notice then given to the industry were "to that extent, excessive and unjustified."

40. "We do agree with Chicago, however, that it should not have to bear the loss resulting from the time that has elapsed since our decision a year ago in *Alabama-Tennessee*. We think the most equitable resolution of this matter is to put Natural on a par with *Alabama-Tennessee*."

41. *Niagara Mohawk Power Corp.* v. *FPC*, *supra* (slip opin. p. 13).

Natural would have no cause for complaint over the 1964 date if in 1964 the Commission had proceeded by way of a policy regulation. On this record it shows no substantial ground for a difference in result because the agency declared a general principle in the context of an individual proceeding, but with leave to the industry to participate amicus curiae; it was free to utilize this technique notwithstanding the efforts of courts and scholars to encourage greater use of regulations for broad policy declaration.[42] Satisfied that its findings were valid with respect to *Alabama-Tennessee* "and other typical pipelines" the Commission left a gas pipeline not a party to that proceeding "legally free to introduce evidence and testimony of exceptional situations demonstrating the inapplicability of the determinations made in Opinion No. 417 to its individual situation."[43] That left a pipeline free to try to be excused, but did not require a postponement of the effective date for a company like Natural that did not even make an effort to claim its individual situation was "exceptional." *New England Divisions case,* 261 U. S. 184, 199 (1923). A contrary requirement would breed litigation for the sole purpose of delay.

This leads us into a discussion of Natural's thorny contention that it is entitled to an October 1965 effective date because dates in this general range are reflected in the orders, with prospective effect, entered with regard to other companies. Certainly Natural is entitled to relief if it has been singled out for a difference in treatment not justified by a difference in conditions.[44] And Natural points out

42. *SEC* v. *Chenery Corp.,* 332 U. S. 194, 202-03 (1947); *Alabama-Tennessee Natural Gas Co.* v. *FPC,* 359 F. 2d at 343; *International Union of Operating Eng'rs* v. *NLRB,* 122 U. S. App. D. C. 314, 318, 353 F. 2d 852, 856 (1965).

43. Opinion 417A, *Alabama-Tennessee Natural Gas Co.,* 31 F. P. C. 928, 930 (1964) (on rehearing).

44. *McKay* v. *Wahlenmaier,* 96 U. S. App. D. C. 313, 226 F. 2d 35 (1955).

that Opinion 417, the *Alabama-Tennessee* opinion, after phrasing the issues, stated that the issue had been reserved in other cases, where "we uniformly provided that any changed policy . . . would have only a prospective effect on the rates and charges of the individual pipelines concerned." In a footnote Natural's case was listed along with three other cases where the ultimate result was prospective from a 1965 effective date.[45]

We find somewhat disingenuous the Commission's observation that the reference to the present proceeding in Opinion 417 conveys no more than that the same issue was presented in both cases. But we do agree that the description of the present proceeding, in the course of an introductory background, was not a commitment to make the present order effective as of the date of its issuance. The settlement obviously contemplated some refund if the liberalized depreciation issue was decided on the merits contrary to Natural's position. We think the Commission decided in accordance with the spirit of both the settlement and the forecast that a change in policy would be "prospective" by its decision under review making the change prospective from an effective date of February 3, 1964.

When we turn to the question of discrimination in factual results, we find that the proceedings listed by Natural involved sufficient differences in posture to negative the charge of arbitrary discrimination. All of the cases involved either a section 5(a) proceeding, in which the Commission has no statutory authority to order refunds and can act only prospectively,[46] or they involved section 4(e)

45. Opinion 417, *supra*, 31 F. P. C. at 209.

46. *Midwestern Gas Transmission Co.*, 32 F. P. C. 993 (1964). In this opinion (No. 444), the Commission ordered a further hearing to determine whether or not use of liberalized depreciation would be proper in computing the tax element of prospective cost of service, at which hearing Midwest would have opportunity to show why, starting in 1963, it used straight line depreciation in

proceedings in which rate reductions were put forward that included but were not limited to the reductions implementing flow throughs.[47]

The proposals were settlements consented to by consumers, cities, and state commissions. Agreed reductions and settlements may involve compromises that recognize that immediate reductions may be preferable to larger refunds sometime in the future.[48] Refunds are not an adequate substitute for an immediate rate reduction. *FPC* v. *Tennessee Gas Transmission Co.*, 371 U. S. 145, 154-55 (1962). As to the Commission's order approving the joint rate reduction offer of *American-Louisiana* and *Michigan-Wisconsin*, affiliated companies which were cited along with Natural in the footnote in Opinion 417, the Commission's opinion under review noted that in those cases, unlike Natural, no evidence had been introduced on treatment of liberalized depreciation and a further evidentiary hearing would have been required, which was not the case as to Natural where no compromise was required in order to avoid delay in implementation, and also that reductions were proposed as to the rates payable by the consumers (to Michigan-Wisconsin).

Though the various Commission's actions have been, so to speak, reconciled so as to avoid the taint of illegal discrimination, we acknowledge an uneasiness that may well

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its tax return. The deferral of the ruling on Midwestern is not inconsistent with requiring use of lower actual tax payments for a utility, like Natural, that used liberalized depreciation on its tax returns. It rather presents a different issue, whether and under what circumstances the Commission may or should utilize a tax component lower than Federal taxes actually paid.

47. *E.g.*, *Panhandle E. Pipe Line Co.*, 31 F. P. C. 736 (1964); *Trunkline Gas Co.*, 31 F. P. C. 743 (1964). See also note 46.

48. *American Louisiana Pipe Line Co.*, 31 F. P. C. 1579 (June 23, 1964). The reduction on other matters by Michigan-Wisconsin could be taken into account in considering whether the public interest warranted acceptance of a joint proposal by that company and its affiliated supplier.

have its roots in the fact that the Commission's general policies were implemented in individual proceedings. The Commission followed up Opinion 417 with an accounting regulation, and charges of discrimination could have been obviated at the start by use of policy regulations both for restatement of the principles of the policy decisions and crystallization of implementing sub-principles. The continued expressions of courts and commentators stressing the desirability of generalized approaches to generalized problems (*supra* note 40), does not betoken a desire to meddle with administrative details and techniques, but rather an uneasiness lest an excessively individuated approach may be a seed bed that is too favorable to the rank weed of discrimination.[49] Judicial development of principles on a case-by-case approach is not a parallel because the courts cannot ordinarily call upon the legislative techniques available with a little effort to agencies, to canvass the range of problems and cases pending and to formulate generalized approaches for their disposition. Yet there are competing considerations that the courts cannot fully assess and in the last analysis the courts cannot invalidate the individuated techniques and results if they have not been shown to be arbitrary or discriminatory. Our conclusion here is that the showing requisite for nullification has not been made.

B. Contention Based on Settlement Agreement.

Chicago and Wisconsin present an alternative contention that the Settlement Agreement mandates application of the flow-through decision, either way, and refunds if any, as of March 1, 1961, the date Natural's increased rates became

49. Compare H. Friendly, the Federal Administrative Agencies: The Need for Better Definition of Standards (1962) passim. Judge Friendly concludes that the case-by-case technique of the CAB muddied the waters so as to retard rather than advance the development of an overall policy approach to the problem of route structure (p. 105).

effective. We agree with the dissenting commissioner who found this contention persuasive on the general point that Natural may properly be held to its bargain even if it turned out badly. It was the prospect of holding Natural to this supposed bargain that apparently led the Joint Petitioners to agree with Natural that the Settlement Agreement did not reserve the issue of rate base reduction. But we do not read the Settlement Agreement as they do. Unlike the issue of rate base reduction previously discussed, the Settlement Agreement clearly does call on the Commission to issue a decision on the issue of Federal tax expense allowances. The parties said in effect: On this issue we cannot work out a settlement, and we leave it to the Commission to decide. The parties may well have assumed that any flow-through decision would be retroactive to 1961, they may have wholly failed to anticipate the possibility that the decision would be prospective, but they did not purport to fetter the Commission's discretion to make its decision prospective. In reaching its decision on the issues referred to it, the Commission was free to announce and apply the principles it deemed proper under the Natural Gas Act just as if it were disposing of a proceeding in which there had been no settlement. We have already upheld, as in accordance with its discretion under the Natural Gas Act, the Commission's decision, not only to provide for a "flow through" policy, but also to prescribe a 1964 effective date therefor. We do not think the Settlement prohibited application of that approach to Natural.

Although in general we have upheld the Commission's findings and action, our ruling in one aspect requires that its order be vacated and the case remanded for further proceedings.

So ordered.

APPENDIX B.

Before: Burger, Tamm and Leventhal, Circuit Judges, in Chambers.

ORDER.

On consideration of the motion of petitioners in case number 19,604 to stay the transmittal of the opinion and certified copy of this Court's judgment and of the responsive pleadings filed with respect thereto, and on consideration of the motion of Natural Gas Pipeline Company of America in case number 19,836 for leave to file a petition for rehearing, the time having expired, it is

Ordered by the Court that the aforesaid motion for stay be granted, and the Clerk is directed to withhold transmittal of the opinion and certified copy of the judgment in case number 19,604 for a period of thirty days from the date of this order, and it is

Further Ordered by the Court that the Clerk is directed to file the lodged petition for rehearing submitted by *Natural Gas Pipeline Company of America,* and on consideration whereof, it is

Ordered by the Court that said petition for rehearing is denied.

Per Curiam.

Dated October 31, 1967.

APPENDIX C.

Administrative Procedure Act, Act of June 11, 1946, c. 324:

SEC. 5. In every case of adjudication required by statute to be determined on the record after opportunity for an ageney hearing, except to the extent that there is involved (1) any matter subject to a subsequent trial of the law and the facts de novo in any court; (2) the selection or tenure of an officer or employee of the United States other than examiners appointed pursuant to section 1010 of this title; (3) proceedings in which decisions rest solely on inspections, tests, or elections; (4) the conduct of military, naval, or foreign affairs functions; (5) cases in which an agency is acting as an agent for a court; and (6) the certification of employee representatives.

* * * * * *

(b) The agency shall afford all interested parties opportunity for (1) the submission and consideration of facts, arguments, offers of settlement, or proposals of adjustment where time, the nature of the proceeding, and the public interest permit, and (2) to the extent that the parties are unable so to determine any controversy by consent, hearing, and decision upon notice and in conformity with sections 1006 and 1007 of this title. [60 Stat. 239; 5 U. S. C. § 1004.]

SEC. 8(b). Prior to each recommended, initial, or tentative decision, or decision upon agency review of the decision of subordinate officers the parties shall be afforded a reasonable opportunity to submit for the consideration of the officers participating in such decisions (1) proposed findings and conclusions, or (2) exceptions to the decisions or recommended decisions of subordinate officers or to ten-

tative agency decisions, and (3) supporting reasons for such exceptions or proposed findings or conclusions. The record shall show the ruling upon each such finding, conclusion, or exception presented. All decisions (including initial, recommended, or tentative decisions) shall become part of the record and include a statement of (1) findings and conclusions, as well as the reasons or basis therefor, upon all the material issues of fact, law, or discretion presented on the record; and (2) the appropriate rule, order, sanction, relief, or denial thereof. [60 Stat. 242; 5 U. S. C. § 1007(b).]

Natural Gas Act, Act of June 21, 1938, c. 556.

SEC. 1. (a) As disclosed in reports of the Federal Trade Commission made pursuant to Senate Resolution 83 (Seventieth Congress, first session) and other reports made pursuant to the authority of Congress, it is hereby declared that the business of transporting and selling natural gas for ultimate distribution to the public is affected with a public interest, and that Federal regulation in matters relating to the transportation of natural gas and the sale thereof in interstate and foreign commerce is necessary in the public interest. [52 Stat. 821 (1938); 15 U. S. C. § 717 (a)].

SEC. 4. (a) All rates and charges made, demanded, or received by any natural-gas company for or in connection with the transportation or sale of natural gas subject to the jurisdiction of the Commission, and all rules and regulations affecting or pertaining to such rates or charges, shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful.

(b) No natural-gas company shall, with respect to any transportation or sale of natural gas subject to the juris-

diction of the Commission, (1) make or grant any undue preference or advantage to any person or subject any person to any undue prejudice or disadvantage, or (2) maintain any unreasonable difference in rates, charges, service, facilities, or in any other respect, either as between localities or as between classes of service.

(c) Under such rules and regulations as the Commission may prescribe, every natural-gas company shall file with the Commission, within such time (not less than sixty days from the date this act takes effect) and in such form as the Commission may designate, and shall keep open in convenient form and place for public inspection, schedules showing all rates and charges for any transportation or sale subject to the jurisdiction of the Commission, and the classifications, practices, and regulations affecting such rates and charges, together with all contracts which in any manner affect or relate to such rates, charges, classifications, and services.

(d) Unless the Commission otherwise orders, no change shall be made by any natural-gas company in any such rate, charge, classification, or service, or in any rule, regulations, or contract relating thereto, except after thirty days' notice to the Commission and to the public. Such notice shall be given by filing with the Commission and keeping open for public inspection new schedules stating plainly the change or changes to be made in the schedule or schedules then in force and the time when the change or changes will go into effect. The Commission, for good cause shown, may allow changes to take effect without requiring the thirty days' notice herein provided for by an order specifying the changes so to be made and the time when they shall take effect and the manner in which they shall be filed and published.

(e) Whenever any such new schedule is filed the Commission shall have authority, either upon complaint of any

State, municipality, or State commission, or upon its own initiative without complaint, at once, and if it so orders, without answer or formal pleading by the natural-gas company, but upon reasonable notice, to enter upon a hearing concerning the lawfulness of such rate, charge, classification, or service; and, pending such hearing and the decision thereon, the Commission, upon filing with such schedules and delivering to the natural-gas company affected thereby a statement in writing of its reasons for such suspension, may suspend the operation of such schedule and defer the use of such rate, charge, classification, or service, but not for a longer period than five months beyond the time when it would otherwise go into effect: *Provided,* That the Commission shall not have authority to suspend the rate, charge, classification, or service for the sale of natural gas for resale for industrial use only; and after full hearings, either completed before or after the rate, charge, classification, or service goes into effect, the Commission may make such orders with reference thereto as would be proper in a proceeding initiated after it had become effective. If the proceeding has not been concluded and an order made at the expiration of the suspension period, on motion of the natural-gas company making the filing, the proposed change of rate, charge, classification, or service shall go into effect. Where increased rates or charges are thus made effective, the Commission may, by order, require the natural-gas company to furnish a bond, to be approved by the Commission, to refund any amounts ordered by the Commission, to keep accurate accounts in detail of all amounts received by reason of such increase, specifying by whom and in whose behalf such amounts were paid, and, upon completion of the hearing and decision, to order such natural-gas company to refund, with interest, the portion of such increased rates or charges by its decision found not justified. At any hearing involving a rate or charge sought to be

increased, the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the natural-gas company, and the Commission shall give to the hearing and decision of such questions preference over other questions pending before it and decide the same as speedily as possible. [52 Stat. 822 (1938); 15 U. S. C. § 717c].

SEC. 5. (a) Whenever the Commission, after a hearing had upon its own motion or upon complaint of any State, municipality, State commission, or gas distributing company, shall find that any rate, charge, or classification demanded, observed, charged, or collected by any natural-gas company in connection with any transportation or sale of natural gas, subject to the jurisdiction of the Commission, or that any rule, regulation, practice, or contract affecting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory, or preferential, the Commission shall determine the just and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order: *Provided, however,* That the Commission shall have no power to order any increase in any rate contained in the currently effective schedule of such natural-gas company on file with the Commission, unless such increase is in accordance with a new schedule filed by such natural-gas company; but the Commission may order a decrease where existing rates are unjust, unduly discriminatory, preferential, otherwise unlawful, or are not the lowest reasonable rates.

(b) The Commission upon its own motion, or upon the request of any State commission, whenever it can do so without prejudice to the efficient and proper conduct of its affairs, may investigate and determine the cost of the production or transportation of natural gas by a natural-gas company in cases where the Commission has no au-

thority to establish a rate governing the transportation or sale of such natural gas. [52 Stat. 823 (1938); 15 U. S. C. § 717d].

SEC. 19. (b) Any party to a proceeding under this act aggrieved by an order issued by the Commission in such proceeding may obtain a review of such order in the circuit court of appeals of the United States for any circuit wherein the natural-gas company to which the order relates is located or has its principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the order of the Commission upon the application for rehearing, a written petition praying that the order of the Commission be modified or set aside in whole or in part. A copy of such petition shall forthwith be transmitted by the clerk of the court to any member of the Commission and thereupon the Commission shall file with the court the record upon which the order complained of was entered, as provided in section 2112 of title 28, United States Code. Upon the filing of such petition such court shall have jurisdiction, which upon the filing of the record with it shall be exclusive, to affirm, modify, or set aside such order in whole or in part. No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do. The finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. If any party shall apply to the court for leave to adduce additional evidence, and shall show to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for failure to adduce such evidence in the proceedings before the Commission, the court may order such additional evidence to be taken before the Commission and to be adduced

upon the hearing in such manner and upon such terms and conditions as to the court may seem proper. The Commission may modify its findings as to the facts by reason of the additional evidence so taken, and it shall file with the court such modified or new findings, which if supported by substantial evidence, shall be conclusive, and its recommendation, if any, for the modification or setting aside of the original order. The judgment and decree of the court, affirming, modifying, or setting aside, in whole or in part, any such order of the Commission, shall be final, subject to review by the Supreme Court of the United States upon certiorari or certification as provided in [former] sections 239 and 240 of the Judicial Code, as amended (U. S. C., title 28, sec. 1254). [52 Stat. 831 (1938), as amended 15 U. S. C. § 717r(b) (1958)].

Fifth Amendment United States Constitution.

No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a Grand Jury, except in cases arising in the land or naval forces, or in the Militia, when in actual service in time of War or public danger; nor shall any person be subject for the same offense to be twice put in jeopardy of life or limb; nor shall be compelled in any criminal case to be a witness against himself, nor be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation.

APPENDIX D.

Ross, McGowan, Hardies & O'Keefe.
122 South Michigan Avenue, Chicago 3.

May 10, 1962.

Mr. John C. Melaniphy,
Corporation Counsel,
City of Chicago,
City Hall,
Chicago, Illinois.

Dear Mr. Melaniphy:

Pursuant to your request, there is attached to this letter a copy of the language to be used in the settlement agreement of the current FPC rate case of Natural Gas Pipeline Company of America. This language covers the purchase gas cost reduction problem which you and Mr. Danaher discussed with Mr. Brackett and me.

May I first point out that the full agreement in the case provides that Natural has accepted the cost of service proposed by the FPC staff, and Natural unconditionally agrees to make refunds of all sums collected *in the past* in excess of that cost of service. That includes an obligation to make roughly a $3,000,000 refund for Chicago consumers. Natural also unconditionally agrees to reduce its *future* rates to reflect that decreased cost of service.

Natural also agrees to go to trial before the FPC on two issues and if it loses on either, to make *additional refunds and rate reductions* (over and above the unconditional ones mentioned above). As you recall, one of these issues which will go to trial—the normalization of taxes—is going to trial at your request.

Natural also agrees that if the Texas Pipeline Tax is declared invalid, Natural will make the proper refund. And if no other taxes replace the invalid tax, Natural will make the appropriate rate reduction. This is the proposal made by the City of Chicago, which Natural has agreed to. And again, this rate reduction and refund from the Texas Tax is in addition to those mentioned earlier.

That leaves only the question of Natural's cost of gas it purchases from the oil and gas companies, which was discussed with you yesterday. Natural's proposal—which has been agreed to by the FPC staff and other parties, except the City—is as follows:

Whenever a decrease in the rates of any of Natural's suppliers used in this case occurs, Natural will then see if the increase from other such suppliers since 1960, the starting point in this case, are more or less than those decreases. If there has been a net decrease, Natural will reduce its rates. But if there has been a net increase, it will not reduce Natural's rate, but, of course, it will also not be free to increase them during the moratorium. This would work this way.

Assume that only two companies sell gas to Natural. Assume that Supplier A is required to *reduce* his rates so that it reduces Natural's cost of gas by $500,000 per year. Assume that Supplier B has *increased* his rates so that it increased Natural's cost of gas by $200,000 per year. Then Natural must decrease its own rates by $300,000 per year.

If there had been no increase in the rates of Supplier B, then Natural would reduce its rates by *$500,000.*

If the rates of Supplier B had *increased $1,000,000,* Natural's rates would *not* increase.

In other words, when the decrease in Supplier A's rates occurs, Natural will then see if its net cost of gas from both Supplier A and B has gone up or down. If it has gone up,

Natural's rates will not increase. If its net cost of gas from both Supplier A and B has gone down, Natural will reduce its rates by that amount.

We believe this is more than fair. Natural will itself pay for the net increased costs of gas it suffers. But it will pass the net decreases on to its customers.

However, Mr. Wiskup has demanded that whenever Supplier A's rates go down $500,000, Natural must reduce its rates by that amount, *even though Supplier A has increased his rates $1,000,000.* Thus, Mr. Wiskup has demanded that Natural reduce its rates at a time when its *overall cost of gas* has increased.

We believe that his position is clearly unreasonable.

As I said before, the position Mr. Wiskup took on this point is the only thing now holding up the completion of the settlement agreement, which will lead to refunds by Natural. The technical language which expresses Natural's proposal, which I described above, is attached to this letter. If you will approve this proposal, Natural will immediately submit the entire agreement, including that language, to you (or your representative) and to the FPC staff for final agreement. Since all other parts of the agreement have been approved in principle previously, the rest of the steps should move along swiftly.

If you have any questions, please do not hesitate to get in touch with Mr. Brackett or me. I will call you tomorrow afternoon to see if you approve this proposal.

With best regards, I am

Very truly yours,

CARL MCGOWAN.

Att.

cc: Mr. James Danaher.

APPENDIX E.

FEDERAL POWER COMMISSION.

Re Natural Gas Pipeline Company of America.

Opinion No. 367, Docket No. RP61-8

October 25, 1962.

By the COMMISSION: Natural Gas Pipeline Company of America, its customers, the city of Chicago, the Wisconsin Public Service Commission, and the staff have agreed upon a rate settlement[1] and have submitted it for our approval. The settlement arises out of a § 4(e), 15 U. S. C. A. § 171c (e), proceeding and was negotiated after a full hearing but before briefs were submitted to the examiner. It reduces Natural's annual increment in rates above those established by previous settlements[2] from a proposed $12,600,000 to $6,200,000. If the settlement is approved refunds exceeding $8,800,000 will be made covering the period from March 1, 1961, when Natural began collecting the filed rates under bond until the date upon which the agreement becomes effective.

The parties to the agreement have left two contested issues for our subsequent decision: The first is whether Natural should include in its cost of service federal income tax expense computed at 52 per cent of its taxable income or computed at the consolidated company's effective tax rate. The second issue is whether Natural should "normalize" its tax expense to eliminate the effect of Internal Revenue

1. The text of the settlement appears at Tr. 2945-70 and is incorporated by reference. The proposed rates are set forth in Appendix A [omitted herein].

2. Docket Nos. G-18148, G-18149, and RP 60-5.

Code § 167, 26 U. S. C. A. § 167, relating to accelerated depreciation, or should compute its tax expense on the basis of taxes actually paid during the test year (1960). The settlement provides further that pending our decision on these issues, Natural shall collect revenues subject to refund based upon a 52 per cent tax rate and "normalized" depreciation.[3]

[1] Representatives of the coal industry[4] (hereinafter referred to as interveners) were allowed to, intervene in these proceedings. They have objected to the proposed settlement on the ground that the rate design does not enable Natural to recover through the commodity component of its tariff all expenses classified as commodity costs. Classification of costs between demand and commodity is not a precise mathematical operation but necessarily involves some judgment. Further judgment is required in translating cost allocation results to just and reasonable rates. Here under the Seaboard cost allocation procedure a commodity rate on the settlement cost of service was found to be 22.62 cents. At the other extreme the variable costs associated with the commodity component are approximately 15 cents. The staff initially proposed a commodity rate of 21.37 cents and the company 20 cents. The settlement rate of 20.6 cents is between these amounts and includes considerable fixed costs when compared with the extreme of 15 cents. Interveners assert that the record does not warrant this departure from our decision in Re Atlantic Seaboard Corp. (1952) 11 FPC 43, 94 PUR NS

3. Additional refunds and appropriate rate reductions are required under the agreement if certain producer prices reflected in Natural's cost of service are reduced by commission order and if the Texas dedicated gas reserve tax is invalidated. It was agreed that rate reductions, if any, would be applied to the demand component of Natural's rates.

4. Fuels Research Council, Inc., United Mine Workers of America, Mid-West Coal Producers Institute, Inc.

235, where we held that fixed costs should be allocated 50 per cent to demand and 50 per cent to commodity.

Seaboard did not hold, however, that all commodity costs must be recovered in the commodity component of a pipeline tariff. On the contrary, in Seaboard we said:

". . . While, as we have pointed out, such an allocation of costs is not necessarily controlling in the fixing of the precise level of the demand and commodity components of the rates, they are, in the absence of other mitigating circumstances, a reasonably accurate guide as to the appropriate level for the demand charge and the commodity charge." Re Atlantic Seaboard Corp. *supra*, 11 FPC 43, 62, 94 PUR NS 235, 254.

[2] In the case before us, there are mitigating factors, for the record indicates (1) that Natural's distributor customers would stop taking substantial quantities of gas at rates exceeding 20.6 cents, and (2) that substantial fixed costs are included in the commodity charge.

Natural is in close competition with Midwestern Gas Transmission Corporation, which sells gas to Northern Indiana Public Service Company and to Northern Illinois Gas Company, two of Natural's most important customers. Thus, Northern Indiana's vice president testified that if Natural's commodity charge were raised to 21.37 cents, his company would purchase from Midwestern 5,707,393.7 Mcf of gas it now buys from Natural for resale to Commonwealth Edison. Since Widwestern charges Northern Indiana 20.829 cents per Mcf, we infer that such a shift could occur at any price materially in excess of that amount.[5]

Similarly, an official of Northern Illinois Gas Company estimated that it would purchase 3 million Mcf from Mid-

5. The witness was asked to forecast the impact of a rise in Natural's commodity price to 21.37 cents per Mcf, a rate proposed by the staff prior to settlement. The witness was not asked at what price a shift to Midwestern would occur.

western at 20.642 cents per Mcf in the event Natural's commodity charge were raised to 21.37 cents. We infer that Natural would lose substantial sales at a commodity rate above the proposed 20.6 cents.

In addition, an official of Peoples Gas, Light & Coke Company, another Natural customer, testified that Peoples lost 4 million Mcf in annual sales to Commonwealth Edison Company in 1959, when coal became available at a lower net cost per Btu than Peoples could deliver natural gas. At that time Natural's commodity rate was 20 cents per Mcf. The witness testified further that his company would lose 4,500,000 Mcf annually to coal competition if Natural's commodity charge were raised to 23.62 cents. Some of these sales would probably also be lost at 22.62 cents, since a tabulation placed in the record by this witness comparing Peoples' delivered gas prices with coal prices shows that the 2.62 cents above present rate for which interveners argue would bring certain of Peoples' prices above competing costs for coal. Even at the present 20-cent price, the witness testified, Peoples has been unable to attach new industrial customers. This testimony indicates that an increase to 22.62 cents could lead to further sales losses by Peoples and thus reduce its take from Natural.

Natural's loss of such sales would decidedly not be in the public interest. A 20.6-cent commodity charge which the record indicates approximates the highest commodity rate, which can be fixed without leading at least one customer to shift over 5,700,000 Mcf of its requirements to Midwestern, would include more than 5.6 cents of fixed costs. These would have to be recovered through higher demand or commodity charges to remaining customers in the event sales were lost by a higher commodity rate. These increases, in turn, might result in still further sales losses, and further offsetting rate increases. The impact of the sales losses would be magnified, moreover, by Natural's contractual ob-

ligations to take or pay for a volume of gas closely approximating the sales estimated for the test year in the record. As a result, Natural's remaining customers would have to bear the burden not only of the fixed costs previously borne by the distributor's interruptible customers but also the cost of the gas which would have been utilized for these lost sales. Moreover, to the extent that the distributor's interruptible rates include some fixed costs, loss of interruptible sales may throw those costs back upon the distributor's firm customers.

We, of course, do not hold that in every instance we would necessarily permit a pipeline to reduce its commodity rate to the level of the commodity rate of a competing pipeline. In this connection we note that Midwestern's rate design is subject to review in Docket No. RP61-19. It may be that that review will lead us to order an increase in Midwestern's commodity rates, and thus relieve Natural from some of the competitive pressure which justifies the rate design in this settlement. In light of these circumstances, we propose to reopen the question of Natural's rate design pursuant to our powers under § 5(a), 15 U. S. C. A. § 717d(a), when we reconsider Midwestern's rate design. In the interim, however, we think the record establishes that the 20.6-cent commodity rate proposed in the settlement agreement is just and reasonable.

Having so determined, we will also approve the settlement with respect to the noncontested issues. Our approval is conditioned, however, upon Natural's agreement to a rate adjustment and refund in the event it succeeds in upsetting an Internal Revenue Service ruling disallowing deductions for depreciation of pipeline rights of way. Even though the service's position was rejected in Northern Nat. Gas Co. v. O'Malley (CA 8th 1960) 277 F. 2d 128, taxes included in Natural's cost of service are computed on the assumption that rights of way are not depreciable. Should

this assumption prove erroneous, Natural must pass the resulting tax benefits on to its customers. With that condition, the commission finds, on the basis of the record before it, that the rates proposed in the settlement agreement are just and reasonable, and that their approval is in the public interest.

The commission finds:

(1) The increased rates and charges contained in Second Revised Volumes Nos. 1 and 2 of the Natural Gas Pipeline Company of America's FPC Gas Tariff, filed October 24, 1960, have not been shown to be just and reasonable, or otherwise lawful, under the terms and provisions of the Natural Gas Act, and should be disallowed and denied as hereinafter provided and ordered.

(2) A commodity rate of 20.6 cents for Natural is just and reasonable under the present circumstances.

(3) The settlement of this proceeding on the basis of the proposed settlement agreement submitted by Natural subject to the terms and conditions hereinafter ordered is reasonable, proper, and in the public interest in carrying out the provisions of the Natural Gas Act and such proposed settlement agreement should be approved and made effective as hereinafter provided and ordered.

(4) Based upon the complete record in this proceeding consisting of the testimony and evidence adduced, and the briefs filed by interested parties, the commission finds the level and design of rates as proposed in the subject settlement agreement in the public interest and in accord with the provisions of the Natural Gas Act.

The commission *orders:*

(A) The rates and charges contained in Second Revised Volumes Nos. 1 and 2 to Natural's FPC Gas Tariff filed October 24, 1960, are hereby disallowed.

(B) The settlement of the proceeding in Docket No. RP61-8 as set forth in Natural's proposed settlement agreement is hereby approved and made effective subject to the terms and conditions hereinafter ordered.

(C) Natural shall file, in the manner and within the time specified in Paragraph III of the settlement agreement, revised tariff sheets:

(1) Eliminating from its CD-1 Rate Schedule the 75 per cent load factor minimum bill provision.

(2) Containing the rates set forth in Appendix A [omitted herein] of this order.

(D) Natural shall refund to its customers in the manner and within the time specified in Paragraph III of the settlement agreement the difference between the amounts paid by each customer under the rates which became effective on March 1, 1961, and the amounts which would have been billed each customer under the settlement rates, together with interest thereon computed at 7 per cent per annum.

(E) Natural shall refund all amounts as are indicated by a recomputation of the income tax allowance in its cost of service in this docket if depreciation of transmission rights of way is held an allowable income tax deduction with interest at the rate of 6 per cent per annum for the period in which Natural had the use of such amount prior to payment to the Internal Revenue Service together with all interest, if any, paid thereon by the Internal Revenue Service.

(F) In the event that the Texas dedicated reserve gas tax is declared to be unconstitutional, Natural shall file within twenty-seven months from the date of such invalidation revised tariffs reflecting the invalidation of said tax in accordance with Paragraph IV(3) of the agreement.

(G) In the event that the Texas dedicated gas reserve

tax is found to be unconstitutional, Natural shall refund to its customers all amounts received as a result of the invalidation of said tax, together with interest, received thereon, if any, pursuant to Paragraph IV(3) of the agreement.

(H) Any reduction in the rates of Natural's suppliers which results in an ultimate decrease to Natural in excess of subsequent increases by said suppliers shall require Natural to file a reduction in the demand component of its rates and in its straight-line rates and to make appropriate refunds pursuant to Paragraph IV(3) of the agreement. Natural shall not be required to file such reductions until the accumulated net decrease from said suppliers totals $250,000 annually.

(I) Within thirty days from the date of issuance of this order, Natural shall file, in writing and under oath, by a qualified officer or officers of the company, its acceptance of the terms and provisions of this order.

(J) The approval of this agreement and the issuance of this order is without prejudice to any finding or determination that may be made in any further proceedings in this docket or in any other proceeding presently being heard, now pending, or hereinafter instituted by or against Natural Gas Pipeline Company of America.

APPENDIX F.

Settlement Agreement.

Section IV(2)—The question of whether Natural, in computing its cost of service for rate purposes, should compute its Federal income tax expense allowance by "normalizing" such taxes to eliminate the effect of Section 167 of the Federal Internal Revenue Code which relates to "accelerated" or "liberalized" depreciation, or by utilizing the principle of "flow through" of the tax effect of the use of such "accelerated depreciation" deductions for tax purposes, as proposed and defined by the City of Chicago in these proceedings, rather than the "normalization" method, shall be determined by an adjudication by the Commission in these proceedings and this issue shall not be terminated by approval of the settlement proposed hereunder.

To permit a resolution of this issue at the earliest possible date, however, all parties hereto request that in lieu of any intermediate decision proceedings herein, the Commission render a final decision with respect to such issue and, pursuant to the requirements of Section 1.30(c) of the Commission's Rule of Practice and Procedure, request the opportunity to file briefs relating to this issue, inclusive of proposed findings and conclusions, in accordance with a briefing schedule to be prescribed by the Commission, and to thereafter present oral argument to the Commission relating thereto; each party, subject to the aforegoing, reserving its right to apply for rehearing and petition for judicial review of the Commission's decision with respect to such issue.

In the event it shall be determined in these proceedings by a valid and final order of the Commission that Natural in computing its cost of service in these proceedings, must utilize the above mentioned "flow through" method of tax computation, Natural, subject to its right to seek judicial review thereof, *shall make such further refunds, with interest at 7% per annum from the 20th day of each month in which each excess payment was collected,* to the date Natural refunds such excess payments, as shall result from the reduction, if any, in the level of any of the rates contained in its FPC Rate Schedules that may be required by the Commission at the time of such order; provided, however, that Natural's obligation to make a refund hereunder shall not become effective unless and until the aggregate sum refundable under this Paragraph (2) shall be equal to $100,000.

It is agreed that the difference between the depreciation deduction used in computing the Federal Income Tax allowance by use of the above mentioned "normalization" method, which is included in the cost of service of $137,-014,823 and the depreciation deduction for such tax allowance purposes, relative to such cost of service, which would have resulted from use of the above mentioned "flow through" method, is $7,928,320. *Any refunds and/or rate reductions made by reason of this Section IV(2) shall be made as described in the last paragraph of Section IV(1) above.* (Emphasis added.)

* * * * *

APPENDIX G.

Opinion No. 456.

Opinion and Order Determining Applicability of Liberalized Depreciation and Refunds.

(Issued March 18, 1965.)

Swidler, Chairman:

In our Opinion No. 367, 28 FPC, on October 25, 1962, approving the recent settlement of a rate case in these proceedings the Commission reserved the question of the proper treatment for ratemaking purposes of the higher deductions from Federal income taxes made available by liberalized depreciation under Section 167 of the Internal Revenue Code. In *Alabama-Tennessee Natural Gas Co.*, 31 FPC ....., Opinion No. 417, Docket Nos. G-5471, *et al.*, February 3, 1964, the practice of normalization, formerly permitted by the Commission,[1] was found no longer justified with respect to that Company. The initial question is whether the principles of *Alabama-Tennessee* are applicable to Natural. If we conclude that they are, the question here arises as to the date on which the flow-through treatment of liberalized depreciation adopted in *Alabama-Tennessee* is to be made effective for Natural and the amount of any refunds which Natural must make to its customers in the Chicago area.

This proceeding began as a Section 4 rate case. After the hearings ended, a settlement agreement was reached and made part of the record on June 21, 1962 (Tr. 2954). In the settlement the question of the appropriate treat-

1. *Amere Gas Utilities Co.*, 15 F. P. C. 781, and *El Paso Natural Gas Co.*, 22 F. P. C. 260, 267.

ment of liberalized depreciation and consolidated taxes was reserved. We approved the agreement in Opinion No. 367, 28 FPC 731, on October 25, 1962. On May 11, 1964, the City of Chicago filed a motion requesting that the Commission decide the liberalized depreciation issue, and on May 19, 1964, Natural filed its answer and a proposal to reduce its rates as of October 1, 1965, stating that it was willing to waive its right to conduct further proceedings to show cause why the determination in *Alabama-Tennessee* is not applicable to Natural if the Commission approved its proposal. Under the proposal Natural's reduced rates would reflect the holding in *Alabama-Tennessee*. Thus, in computing its rates Natural would deduct the balance of deferred taxes in Account 282 from its rate base and would flow-through the tax reduction resulting from liberalized depreciation unless it elected to abandon use of liberalized depreciation by October 1, 1965. Natural also proposed that the rate reduction would be deferred beyond October 1, 1965, until *Alabama-Tennessee* became final, but, if so, Natural would pay a refund from that date if the Commission were upheld. Chicago objected to the rate reduction proposal arguing that the utilization of liberalized depreciation by Natural should in accordance with the principles enunciated in *Alabama-Tennessee* be flowed through to its customers and under the settlement agreement Natural should put its rate reduction in effect as of March 1, 1961.

In our order of July 31, 1964, we recited that Natural had filed a rate reduction proposal, in which it had waived its right to contest the applicability of *Alabama-Tennessee* to it if we approved the proposal. The order makes clear, however, that the reopened proceeding was not limited to consideration of Natural's proposal and provided broadly for the filing of briefs on all questions relating to the reserved issue of liberalized depreciation. Briefs were ac-

cordingly filed by Natural, our staff, and Chicago, whose brief the Public Service Commission of Wisconsin adopts.

Initially, it is clear that we must determine whether the principles of *Alabama-Tennessee* are applicable to Natural. The settlement agreement calls for determination of this question, and our order of July 31, 1964, required briefs on it. Natural did not submit additional evidence on the question, and did not argue the question in its briefs, although our order gave it opportunity, and indeed called for such argument. The hearing record in the case made prior to the original settlement contains undisputed evidence showing that, like the pipeline industry as a whole, Natural is an expanding enterprise, and will continue to expand in the foreseeable future. Natural apparently does not dispute the fact it is properly subject to the principles enunciated in *Alabama-Tennessee* if that case is upheld. As with *Alabama-Tennessee*, we are of the opinion that flow-through and lower rates are a more effective stimulus to new investment than normalization, and, as in that case, we shall provide for deduction of the accumulated reserves from the rate base, unless Natural submits an appropriate plan for flowing some or all of such reserves through to its customers.

We now turn to the question as to the date on which Natural should give effect to these principles. All parties agree that the settlement agreement represents a binding contract; the controversy arises over its effect. The agreement provides in Section IV(2) as follows:

> 2. The question of whether Natural, in computing its cost of service for rate purposes, should compute its federal income tax expense allowance by "normalizing" such taxes to eliminate the effect of Section 167 of the Federal Internal Revenue Code, which relates to "accelerated" or "liberalized" depreciation, or by utilizing the principle of "flow-through" of the tax effect of the use of such "accelerated depreciation"

deductions for tax purposes, as proposed and defined by the City of Chicago in these proceedings, rather than the "normalization" method, shall be determined by an adjudication by the Commission in these proceedings and this issue shall not be terminated by approval of the settlement proposed hereunder.

To permit a resolution of this issue at the earliest possible date, however, all parties hereto request that in lieu of any intermediate decision proceedings herein, the Commission render a final decision with respect to such issue and, pursuant to the requirements of Section 1.30(c) of the Commission's Rules of Practice and Procedure, request the opportunity to file briefs relating to this issue, inclusive of proposed findings and conclusions, in accordance with a briefing schedule to be prescribed by the Commission, and to thereafter present oral argument to the Commission relating thereto; each party, subject to the foregoing, reserving its right to apply for rehearing and petition for judicial review of the Commission's decision with respect to such issue.

In the event it shall be determined in these proceedings by a valid and final order of the Commission that Natural, in computing its cost of service in these proceedings, must utilize the above mentioned "flow through" method of tax computation, Natural, subject to its right to seek judicial review thereof, shall make such further refunds, with interest at 7 per cent per annum from the 20th day of each month in which each excess payment was collected, to the date Natural refunds such excess payment, as shall result from the reduction, if any, in the level of any of the rates contained in its FPC Rate Schedules that may be required by the Commission at the time of such order; provided, however, that Natural's obligation to make a refund hereunder shall not become effective unless and until the aggregate sum refundable under this Paragraph (2) shall be equal to $100,000.

It is agreed that the difference between the depreciation deduction used in computing the Federal Income Tax allowance by use of the above mentioned "normalization" method, which is included in the cost of serv-

ice of $137,014,823, and the depreciation deduction for such tax allowance purposes, relative to such cost of service, which would have resulted from use of the above mentioned "flow through" method, is $7,928,320. Any refunds and/or rate reductions made by reason of this Section IV (2) shall be made as described in the last paragraph of Section IV (1) above.

In interpreting this agreement both Chicago and the staff argue that it provides for a full refund for the entire period that excess rates were collected. They contend that the treatment of liberalized depreciation was the issue reserved, and, once it is decided that normalization is improper, Natural's cost of service should be adjusted and refunds should follow automatically from March 1, 1961. Natural on the other hand contends that there should be no refunds prior to October 1, 1965, assuming that the Commission is upheld by the Courts in *Alabama-Tennessee.*

It is entirely clear to us that the agreement was drafted with the possibility of refunds in mind. Thus it is provided that "In the event it shall be determined" that Natural must use "flow-through", it "shall make such further refunds . . . as shall result from the reduction, if any, in the level of any of the rates contained in its FPC Rate Schedules that may be requested by the Commission. . . ." However, it is also clear that the refund is made contingent on the action we might take on the question of liberalized depreciation and there is no language in the settlement which can fairly be interpreted as requiring us to order refunds retroactive to the date the rate increase was put into effect by Natural.

Chicago cites a letter of May 10, 1962, written to its corporation counsel by counsel for Natural explaining the proposed settlement agreement. There it is stated that "Natural also agrees to go to trial before the FPC on two issues and if it loses on either, to make additional refunds

and rate reductions. . . ." Even if this letter is admissible as an explanation of the settlement agreement, there is nothing in this language which supports a conclusion that the parties agreed on March 1, 1961 as the effective date for making refunds. Under the language of this letter, as in the settlement agreements, the question of refunds is dependent on our decision herein with respect to liberalized depreciation. The question before us is to determine the appropriate date for refunds in light of all of the circumstances of this case.

Opinion No. 367 approving the settlement does not lead to a different result. The relevant language reads as follows (28 FPC at p. 733):

> The second issue is whether Natural should "normalize its tax expense to eliminate the effect of Int. Rev. Code § 167, relating to accelerated depreciation, or should compute its tax expense on the basis of taxes actually paid during the test year (1960). The settlement provides further that pending our decision on these issues, Natural shall collect revenues subject to refund based upon a 52% tax rate and "normalized" depreciation.

This language, like that in the settlement agreement, does not require a refund as of any particular date, although it does contemplate a refund if that should be required by our determination.

Both Natural and Chicago claim support for their position from our decision in *Alabama-Tennessee*. We agree with Chicago that the reference to the present proceeding in Opinion No. 417[2] conveys no more than that the same

2. Opinion No. 417 stated 31 F. P. C. at p. . . . ., Mimeo. Page 2: The same issue was also deferred in a number of Commission orders prescribing future rates for other natural gas pipeline companies, conditioned on the decision in this case.[3] In thus reserving this issue, we uniformly provided that any changed policy which might be formulated in this proceeding would have only a prospective effect on the rates and charges of the

substantive issue was presented in both cases. We also agree that it was not a commitment that we would make any determination here prospective from the date of this order or from the October 1965 date proposed by Natural. On the other hand, there is nothing in this language to suggest that our substantive determination here *must* be made retroactive to March 1, 1961.

The question of the proper treatment of liberalized depreciation is uniquely a matter for the Commission's informed judgment. While we have decided that for the future flow-through should be the normal rate treatment of liberalized depreciation (and the normal accounting treatment as well) and specifically that it should be applied to Natural, our previous treatment of deferred taxes for rate purposes at a 1½ percent rate of return was not illegal. See *Panhandle Eastern Pipe Line Co.* v. *F. P. C.*, 316 F. 2d 659 (CADC), certiorari denied, 375 U. S. 881. If we had chosen to utilize the instant case rather than the *Alabama-Tennessee* proceeding as the vehicle for reconsidering our previous policy, we have applied our new policy of flowing through the tax benefits resulting from

individual pipelines concerned. We are aware that a number of such pipelines have argued in these proceedings that the result we reach here cannot be made binding upon them in the absence of further proceedings. While we are not convinced as to the validity of such arguments, we shall afford such other pipelines an opportunity to show cause why the determination we are making here is not applicable to them. Accordingly, the decision rendered herein will constitute the final element in determining a just and reasonable level of return for *Alabama-Tennessee* and a proposed decision on this point with regard to the various other pipelines with respect to which this specific issue has been reserved.

3. American Louisiana Pipe Line Co. and Michigan Wisconsin Pipe Line Company, Opinion No. 363, issued September 17, 1962; El Paso Natural Gas Company, Opinion No. 366, October 19, 1962; Southern Natural Gas Company, Opinion No. 379, February 18, 1963; Natural Gas Pipe Line Co. of America, RP61-8, Opinion No. 367, October 25, 1962.

the use of liberalized depreciation and deducting the accumulated reserves from the rate base prospectively only as we in fact did in *Alabama-Tennessee*. Nothing in the settlement stipulation or anything else which has been brought to our attention would have required a different conclusion.

We do agree with Chicago, however, that it should not have to bear the loss resulting from the time that has elasped since our decision a year ago in *Alabama-Tennessee*. We think the most equitable resolution of this matter is to put Natural on a par with *Alabama-Tennessee*. We shall therefore order refunds back to February 3, 1964.

Natural's selection of an October 1965 date seems to reflect the view that it is entitled to be put on a par with American-Louisiana, Michigan-Wisconsin, Panhandle and Trunkline rather than Alabama-Tennessee. With respect to each of these four pipelines, rate settlements agreeable to their customers as well as the Commission were subsequently reached, after our decision in *Alabama-Tennessee*, under which they agreed to flow through the benefits of liberalized depreciation commencing in October 1965, subject to the outcome of the pending litigation in *Alabama-Tennessee*.[3] In none of those proceedings did the settlement actually reserve the liberalized depreciation issue or provide that the pipeline agreed to make such refunds as the Commission might order.

In the case of American-Louisiana and Michigan-Wisconsin, unlike Natural, no evidence had been introduced on the question of the treatment of liberalized depreciation, and the issue was confined to whether a return should be al-

3. American Louisiana Pipeline Co., 31 F. P. C. ...., Docket No. G-18419, June 23, 1964; Michigan Wisconsin Pipe Line Co., 31 F. P. C. ...., Docket No. RP64-38, June 23, 1964; Panhandle Eastern Pipe Line Co., 31 F. P. C. ...., Docket No. RP64-18, March 30, 1964; Trunkline Gas Co., 31 F. P. C. ...., Docket No. RP64-19, March 30, 1964.

lowed on accumulated deferred taxes as formerly prescribed in the *Northern Natural* case, 25 FPC 431. A further hearing would have been required before flow-through could be implemented. For that reason the October 1, 1965 date was agreed upon in settlement negotiations (which also provided for certain other reductions in Michigan-Wisconsin's rates) as the date by which a Commission decision on this matter after hearing could have been reached. Thus there was avoided the necessity for such a hearing while *Alabama-Tennessee* was being reviewed in the courts.

With respect to Panhandle and Trunkline, the situation is even less analogous. Neither of these companies were subject to any contingent liability with respect to their use of liberalized depreciation and neither had pending rate increase proceedings. Instead, as a result of informal representations made by the Commission's staff following its review of the pipelines' earnings for calendar year 1963, the two companies, as part of an overall proposal which involved filing immediate rate reductions, agreed also to file further reductions to reflect the flow-through of liberalized depreciation as of October 1965, contingent upon the outcome of the *Alabama-Tennessee* case.

The Commission further finds:

(1) Natural will maintain a growing or stable plant for the foreseeable future.

(2) Rate flow-through will effectively and substantially promote expanded plant investment by Natural and will best implement the fundamental objective of Section 167 of the Internal Revenue Code, to benefit the national economy by stimulating plant modernization and expansion.

(3) Accumulated "deferred tax" balances should be maintained intact and retained by Natural as a contingency reserve (not a segregated fund) and withdrawn only to offset any increased taxes resulting from a decline in overall

tax depreciation deductions, attributable to earlier use of liberalized depreciation, on all depreciable properties used in rendering public service, below the level of the normal tax deductions under straight-line depreciation, or until amortized pursuant to a plan approved by the Commission.

(4) There is no present factual justification for normalizing the rates of Natural after the date of issuance of our Opinion No. 417, *Alabama-Tennessee Natural Gas Co.*, 31 FPC ....., Docket No. G-5471, *et al.*, on February 3, 1964, so that rates should reflect only the actual taxes currently payable based upon the cost of service set forth in the stipulation of June 21, 1962.

(5) Natural is not entitled to any return on accumulated amounts in Account 282, Accumulated Deferred Income Taxes—Liberalized Depreciation, so that amounts included in Account 282 should be exercised from the rate base.

(6) Natural should file reduced rates, and should make refunds for the period commencing February 3, 1964 to reflect the flow-through of tax reductions resulting from the application of Section 167 of the Internal Revenue Code and to reflect the deduction from its rate base of balances in Account 282.

The Commission orders:

(A) Within 30 days of the date that the decision in *Alabama-Tennessee*, Opinion No. 417, becomes final, Natural shall file new rate schedules, effective immediately, reflecting the lower Federal income tax allowance and the lower rate base referred to above conforming to the stipulation of June 21, 1962, and satisfactory to the Commission.

(B) Within 30 days of the date of issuance of the order Natural shall refund to its jurisdictional customers for the period from February 3, 1964, to the date of refund the difference between the amounts collected and those which would have been collected for such period under the rate

schedules required to be filed by this paragraph, together with interest at the rate of 7 percent per annum from the date of payment to Natural to the date of refund.

(C) Within 30 days of making the refunds required by Paragraph (B) Natural shall report to the Commission in writing and under oath the details of its calculations resulting in the refunds together with copies of releases from each of its jurisdictional customers.

By the Commission. Commissioner O'Connor concurring in the result filed a separate statement appended hereto. Commissioner Black dissenting in part filed a separate statement appended hereto.

(Seal)

Joseph H. Gutride,
Secretary.

O'CONNOR, COMMISSIONER, *concurring* in result:

In view of my disagreement with the principles enunciated in *Alabama-Tennessee Natural Gas Co.*, 31 FPC 208 (1964), I am compelled to make a short statement of my position in this proceeding. I adhere to my separate views expressed in that opinion. See my dissenting statement, 31 FPC, at 232, and Commissioner Woodward's dissenting statement, 31 FPC, at 222, with which I expressly joined. Nevertheless, a majority of the Commission endorses that opinion, which is presently being reviewed by the courts. Pending reversal by judicial decision or otherwise, I believe it proper to accept it as the governing expression of Commission policy. Accordingly, I join in consideration of the primary issue in this proceeding: the appropriate date, considering the settlement involved herein, that the policy is to be implemented. For the reasons stated by the majority, I agree that the date applied in *Alabama-Tennessee* should also be followed in this proceeding.

/s/ L. J. O'Connor, Jr.,
Commissioner.

BLACK, Commissioner, *dissenting* in part:

I disagree with the majority opinion because its effect is to withhold from the customers of Natural Gas Pipeline Company in the Chicago area the sum of $28.5 million, plus interest, which rightly belongs to them and to their retail consumers who, for the past four years, have been paying more than they should for gas service. The Commission should order Natural to refund the excess revenues collected by reason of its "normalized" treatment of liberalized depreciation for the entire period the inflated rates have been in effect; that is from March 1, 1961, to the present.

This proceeding was initiated by Natural in October,

1960, under Section 4 of the Natural Gas Act for the purpose of raising its rates. The proposed rates were suspended by Commission action and set for hearing. The suspension period expired and the higher rates became automatically effective March 1, 1961, subject to refund of all amounts collected above the rate which the Commission would, under normal circumstances, determine to be just and reasonable. The parties, however, after full hearing entered into a settlement agreement which the Commission approved in October of 1962, and which provided, *inter alia*, for refund of excess revenues collected from and after March 1, 1961. Not resolved by the parties was the question of the proper rate-making treatment of liberalized depreciation. The settlement agreement by its terms reserved this issue for later determination by the Commission "in these proceedings," and provided that should the Commission decide the "flow-through" method of tax computation to be proper, then Natural would "make such further refunds, with interest at 7 per cent per annum from the 20th day of each month in which each excess payment was collected, to the date Natural refunds such excess payment. . . ."

It is not at all uncommon in settlement proceedings or, for that matter, in fully adjudicated cases, for the parties or the Commission to reserve an issue for subsequent determination. When the severed issue is decided, unless specific provision is made to the contrary, it will relate back in time, utilizing the same test period, and fit into the agreement or the decision of the Commission just as if it had been decided along with the other issues.[1] No contrary intent was evidenced by the parties to the settlement agreement in this case, nor do the circumstances here warrant contrary treatment by the Commission.

1. Cities Service Gas Company, Docket No. G-18799, issued March 27, 1961, 25 F. P. C. 582; Opinion No. 396, issued July 15, 1963, 30 F. P. C. 158.

The majority erroneously relates the refund period here to the *date* of our decision in *Alabama-Tennessee*. While it is true that that decision stands for the proposition that flow-through is the proper rate-making treatment of liberalized depreciation—the same issue that was reserved in the instant case—it was not in the contemplation of the parties that *Alabama-Tennessee* was, as such, the missing piece. They could easily have made such provision in their settlement agreement, but that document doesn't mention *Alabama-Tennessee*. A matter of such vast importance and involving so many millions of dollars in refunds would hardly have been left to inference. If the parties to this case intended that application here of a legal and policy decision to be made some time in the indefinite future in another case, would be prospective from the date that case was decided, clearly they would have said so. It is especially noteworthy that the Commission order in *Alabama-Tennessee* and in the other dockets reserving the issue of liberalized depreciation did expressly provide that its future orders resolving that issue would have prospective effect only.[2]

The Commission rather defensively maintains that while it *could* pick a date earlier than the date *Alabama-Tennessee* was decided for the computation of refunds, it isn't *required* to do so. I disagree. The settlement agreement constitutes a contract which this Commission is not empowered to rewrite for the parties. This case was settled, with our approval, between Natural and its customers on certain definite terms and conditions. One such condition was that should flow-through be decided properly to con-

2. Alabama-Tennessee Natural Gas Company, Opinion No. 360, issued June 13, 1962; American Louisiana Pipe Line Company and Michigan-Wisconsin Pipe Line Company, Opinion No. 363, issued September 17, 1962; El Paso Natural Gas Company, Opinion No. 366, issued October 19, 1962; Southern Natural Gas Company, Opinion No. 379, issued February 18, 1963.

trol Natural's use of liberalized depreciation for rate-making purposes, then Natural would make further refunds reflecting the excess revenues, with interest, from "the 20th day of *each month in which excess payment was collected. . . .*" —not each month after *Alabama-Tennessee* was decided. Indeed, it would seem most unlikely that responsible business management would arrive at an understanding affecting millions of dollars, and leave the measurement of this sum to the uncertain future determination by this Commission of a similar controversy in another case. It may be conceded that the parties, mindful of the pendency of *Alabama-Tennessee,* recognized the necessary applicability of whatever decision the Commission might make in the case, to the facts of the instant case. But it does not follow at all that the *date* of the *Alabama-Tennessee* decision was intended to affect the amount of refunds. Our decision in *Alabama-Tennessee* might have been months away or years away. It is impossible for me to believe that settlement of Natural's rate case was arrived at with such a huge variable intended—one not related to any substantive issue of law, fact, or policy.

This Commission approves settlements only if all the parties agree to the settlement. Here we have approved one settlement on the basis of which the parties discontinued their litigation. We are now, three years later, imposing on them an entirely different "settlement." In my opinion the parties clearly would not have consummated their agreement had they known what would happen to it at the hands of the Federal Power Commission.

It may be that Natural made a bad bargain; but a bargain it was, nonetheless, and it is not incumbent on us to relieve them of it. The majority justifies the result on "equitable" grounds. The gas consumers in the Chicago area who are, in the final analysis, being compelled to bestow a windfall of more than $30 million on Natural Gas

Pipeline Company of America, will surely be surprised to learn that this constitutes "equity" in the view of the Federal Power Commission.

/s/ David S. Black,
Commissioner.

APPENDIX H.

OPINION No. 456-A.

OPINION AND ORDER ON REHEARING.

(Issued June 23, 1965.)

SWIDLER, *Chairman*:

The City of Chicago on April 16, 1965, and Natural Gas Pipeline Company of America on April 19, 1965, have filed applications for rehearing of our Opinion No. 456 and Order issued March 18, 1965. The Public Service Commission of Wisconsin adopts Chicago's application. On May 12, 1965, we granted rehearing for the purpose of further consideration.

After the issue of the treatment of liberalized depreciation as permitted by Section 167 of the Internal Revenue Code had been reserved in a settlement, we determined in Opinion No. 456 that Natural was subject to the principles of *Alabama-Tennessee Natural Gas Co.*, 31 FPC ....., issued February 3, 1964, and must pass along to its customers the advantages of liberalized depreciation. Thus we found that Natural must no longer "normalize" it computation of allowable taxes by computing them on the basis of straight line depreciation, but must "flow through" the advantages of the higher tax deductions to its customers by using the higher liberalized depreciation in computing the tax allowance. We also required that (illegible) Natural to reflect in its rates the deduction of accumulated deferred taxes from its rate base. We ordered Natural to file new rate schedules to carry these changes into effect and make refunds from February 3, 1964, the date *Alabama-Tennessee* was issued.

Natural argues that we have inadvertently erred in ordering the rate base reduction because this issue was terminated by the settlement and was thus not reserved by the terms of the agreement. The City of Chicago agrees that it waived the deduction of the deferred taxes in computing the rate base. In making this statement the City of Chicago was arguing that we had departed from the settlement agreement in reaching our conclusion that refunds should be computed from February 3, 1964. In our opinion both parties are in error.

The settlement agreement, quoted at great length in Opinion No. 456, provides in part as follows:

> 2. The question of whether Natural, in computing its cost of service for rate purposes, should compute its federal income tax expense allowance by "normalizing" such taxes to eliminate the effect of Section 167 of the Federal Internal Revenue Code, which relates to "accelerated" or "liberalized" depreciation, or by utilizing the principle of "flow-through" of the tax effect of the use of such "accelerated depreciation" deductions for tax purposes, as proposed and defined by the City of Chicago in these proceedings, rather than the "normalization" method, shall be determined by an adjudication by the Commission in these proceedings and this issue shall not be terminated by approval of the settlement proposed hereunder.

We were thus required to determine whether Natural should normalize its taxes or flow through the tax effect of liberalized depreciation. Accordingly, we determined that Natural was properly subject to flow-through. This also involved, in our opinion, the proper treatment of the accumulated deferred taxes. These have been accumulated by Natural in Account 282 and represent the difference between normalized taxes and the lower taxes actually paid as a result of the high deductions for liberalized depreciation. The deferred taxes so accumulated thus reflect the

benefits of liberalized depreciation that had not been flowed through to Natural's customers. In fact these accumulations amount to contributions by Natural's customers for taxes not actually paid. There was thus properly before us the rate effects of both the tax computation and the treatment of the amounts in Account 282. Both of these matters were considered and determined in our Opinion No. 417 in *Alabama-Tennessee,* and therefore we prescribed the same solution here as of the date of *Alabama-Tennessee.*

Natural asserts that under the settlement agreement the deferred taxes were treated as a part of capital and a 1.5 percent rate of return allowed on them. Thus Natural argues that the rate base reduction would give cumulative effect to this facet of Commission policy. Natural here is attempting to look behind the figure for cost of service and the rates agreed to in the settlement. The parties however agreed only upon an overall annual cost of service of $137,014,823, based on the calendar year 1960 as adjusted, and made it clear that the "agreement thereto is not intended to reflect agreement to the amount, percentage or method of derivation of any particular item of such cost of service." (Tr. 2956). It was also provided that (Tr. 2967):

> It is expressly understood and agreed that this Stipulation and Agreement is made solely to effect a settlement of these proceedings. Therefore, although the settlement rates listed in Exhibit A are necessarily based on the cost of service agreed upon, this Stipulation and Agreement and attached Exhibit shall not be deemed, *in any other proceeding,* as approval, either by Natural, by any intervenor or by any other party, or any method of principle employed in developing such cost of service or the rates resulting therefrom, or of any specific date used in the computation thereof.

Natural argues that, contrary to *Alabama-Tennessee,* we have made a retroactive application of its principles. Of

course, under Section 4(e) of the Natural Gas Act we are empowered to make our rate order effective back to the date Natural's increased rates became effective subject to refund. We might have done so here except that in *Alabama-Tennessee* we were announcing a new policy and overruling previous decisions. It was therefore not equitable, contrary to the contentions of Chicago, to make our determination effective before February 3, 1964, but on that date the industry was informed of the new policy, and it was appropriate that refunds should be ordered from then.

Natural contends that in reaching this result we have discriminated against it because in other cases we have permitted later dates, but the cases it cites (with one exception), including those referred to in Opinion No. 456, are settlements. Contrary to Natural's argument we think it makes a great deal of difference whether all the terms of a settlement are in one package to be accepted or rejected as in those cases or whether the settlement leaves out an issue to be decided by us as in this proceeding. The one exception cited is *Midwestern Gas Transmission Company,* ..... FPC ....., Opinion No. 444, Docket Nos. RP61-19 and RP62-7, issued October 13, 1964, but this was a *Section 5(a)* proceeding where, of course, we were required to make all rate reductions prospective only.

Natural also points out that on March 29, 1965, after the issuance of Opinion No. 456, it filed an application with the Internal Revenue Service to change, as of January 1, 1965, from the use of liberalized depreciation to the straight-line method for Federal income tax purposes. Therefore, it says, it has no duty to reduce its rates to reflect flow-through for the period beginning January 1, 1965, because it has nothing to flow through for that period. Natural's argument represents an attempt to reopen the record to introduce a new factor in a rate case, which

already has been decided by the Commission. The cost of service based on the test year 1960 was stipulated subject to certain reserved issues including the question of liberalized depreciation for tax purposes. Specifically, the cost of service was stipulated to be $137,014,823; and the settlement agreement reserved the question whether under Section 167 of the Internal Revenue Code the principle of "flow-through" or "normalization" should be used. The record showed and the stipulation assumed that Natural was making use of liberalized depreciation for income tax purposes. For the company now to state that it proposes to abandon use of liberalized depreciation introduces a new fact and a new issue. To bring the record up to date with respect to this one element would destroy the basis of the settlement and would lead to a one-sided result. Where the record is opened to consider one changed element it should be opened for other elements which may have changed in the meantime. *Cf., City of Detroit* v. *F. P. C.*, 230 F. 2d 810 (CADC), *certiorari denied*, 352 U. S. 829.

In order for Natural to give effect to a change in rates resulting from a shift to straight-line depreciation, Natural should make a rate filing in accordance with the provisions of the Act and our regulations. We are not contesting Natural's right to make this change for tax purposes, and we do not propose to suspend such a rate increase for more than one day. In this way a new proceeding will be started, in which other elements in Natural's cost of service can, if appropriate, be put in issue and in which Natural will appropriately have the burden of proof under Section 4(e) to show that its increased rates are just and reasonable, including its use of straight-line depreciation in computing its tax allowance for rate purposes. In the present proceeding we shall require that Natural file new rates thirty days after *Alabama-Tennessee* becomes final based on liberalized depreciation, deduction of the deferred taxes

from the rate base and flow-through. These rates shall be effective from February 3, 1964, until superseded by other rates, presumably the straight-line rates, filed by Natural. We shall require Natural to make refunds reflecting flow-through and the rate base deduction also from February 3, 1964, until the new straight-line rates become effective. In the new proceeding we can require further refunds if it should be determined that Natural is unjustified in employing straight-line tax depreciation for rate-making purposes.

Chicago argues again that the settlement agreement prevents us from prescribing an effective date for the rate reduction other than March 1, 1961, the date the increased rates became effective. As explained in Opinion No. 456, we are of the opinion that the settlement agreement does not require that our substantive determination here *must* be made retroactive to March 1, 1961. Furthermore, there is nothing in Section 4(e) of the Natural Gas Act or the cases cited by Chicago that require us to make our orders retroactive to the date the rate change became effective. Section 4(e) on this matter, provides only that the Commission may "*order such natural-gas* company to refund, with interest, *the portion* of such increased rates or changes by its decision found not *justified.*" *United Gas Co.* v. *Mobile Gas Corp.*, 350 U. S. 332, 341, recognizes our power under Section 4(e) to make our order retroactive to the date the rate change became effective, but it does not require that we do so.

Chicago is correct, however, that our ordering clause (B) is ambiguous and in error, and we accordingly amend it below to clarify it, as well as changing the rate filing and refund provisions to take into account Natural's proposal to abandon liberalized depreciation.

The Commission further finds:

The assignments of error and grounds for rehearing set forth in the applications for rehearing filed in this proceeding present no new facts or legal principles which would warrant any change or modification in the Commission's Opinion No. 456 and Order except as specified below.

The Commission orders:

(A) Our Opinion No. 456 and Order issued March 18, 1965, is hereby confirmed as the decision of the Commission and requests for modification thereof are hereby denied except as provided herein.

(B) For the purpose of reflecting the matters discussed above, particularly Natural's proposal to abandon the use of liberalized depreciation for tax purposes as of January 1, 1965, the ordering clauses of our order of March 18, 1965, are hereby deleted and the following ordering clauses substituted as of the date of issuance of this order.

(C) Within 30 days of the date that the decision in *Alabama-Tennessee,* Opinion No. 417, becomes final, *Natural shall file new rate schedules, effective February 3, 1964,* reflecting the lower Federal income tax allowance and the lower rate base referred to above conforming to the stipulation of June 21, 1962, and satisfactory to the Commission. These rates shall remain effective until the date *superseding rates* filed by Natural become effective.

(D) Within 30 days of the date of issuance of the Commission's order approving the rate filing or filings required by paragraph (C), Natural shall refund to its jurisdictional customers for the period from February 3, 1964, to the date superseding rates become effective, or if there are no superseding rates to the date of refund, the difference between the amounts collected and those which would have been collected for such period under the rate schedules required to be filed by paragraph (C), together with in-

terest at the rate of 7 percent per annum from the date of payment to Natural to the date of refund.

(E) Within 30 days of making the refunds required by paragraph (D), Natural shall report to the Commission in writing and under oath the details of its calculations resulting in the refunds together with copies of releases from each of its jurisdictional customers.

By the Commission.

Commissioner O'Connor concurs in the results only.

Commissioner Black dissenting in part filed a separate statement appended hereto.

(Seal) Commissioner Bagge not participating.

Joseph H. Gutride,
Secretary.

Natural Gas Pipeline Company of America,
Docket No. RP61-8,
(Issued June 23, 1965)

Black, Commissioner, *dissenting in part:*

The matters raised on rehearing strengthen my opinion that the majority is in error on both legal and policy grounds in not requiring Natural to refund the excess revenues collected by reason of its normalized treatment of liberalized depreciation for the entire period the inflated rate has been in effect; that is from March 1, 1961, to the present. I agree, however, with the majority that *Alabama-Tennessee* did not restrict us to a prospective application of its principles. Similarly, I agree that, regardless of the unexpressed intentions of the parties, both Natural and the City of Chicago are in error in concluding that, under their settlement agreement, they had waived the deduction of the deferred taxes in computing the rate base.

David S. Black,
Commissioner.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1967

No. 893

PUBLIC SERVICE COMMISSION OF THE STATE OF WISCONSIN,

and

CITY OF CHICAGO, A MUNICIPAL CORPORATION OF THE STATE OF ILLINOIS,

Joint Petitioners,

vs.

FEDERAL POWER COMMISSION,

Respondent.

On Petition For Writ Of Certiorari To The United States Court Of Appeals For The District Of Columbia Circuit.

BRIEF OF RESPONDENT NATURAL GAS PIPELINE COMPANY OF AMERICA IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

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CITATIONS

Cases:

Alabama-Tennessee Natural Gas Co., 31 FPC 208, affirmed 359 F.2d 318 (5th Cir. 1966), cert. denied 385 U.S. 847 (1966) 3, 7, 15

Public Service Commission of New York v. *F.P.C.*, 329 F.2d 242 (D.C. Cir. 1964), cert. denied, sub nom. *Prado Oil & Gas Co.* v. *F.P.C.*, 377 U.S. 963 (1964) 15

State Corporation Commission of Kansas v. *F.P.C.*, 215 F.2d 176 (8th Cir. 1954) 15

United Gas Improvement Co. v. *Callery Properties, Inc.*, 382 U.S. 223 (1965) 15

United Gas Pipeline Co. v. *Mobile Gas Corp.*, 350 U.S. 332 (1956) 14, 15

Wisconsin v. *F.P.C.*, 303 F.2d 380 (D.C. Cir. 1961), affirmed 373 U.S. 294 (1963) 15

Statutes:

Natural Gas Act, as amended, Section 4(e), 15 U.S.C. 717c(e) 5, 8, 13, 14, 15

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PUBLIC SERVICE COMMISSION OF THE STATE OF WISCONSIN,

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Joint Petitioners,

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FEDERAL POWER COMMISSION,

Respondent.

On Petition For Writ Of Certiorari To The United States Court Of Appeals For The District Of Columbia Circuit.

BRIEF OF RESPONDENT NATURAL GAS PIPELINE COMPANY OF AMERICA IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

Natural Gas Pipeline Company of America (Natural) respectfully requests that this Court deny the Petition for Writ of Certiorari (Petition) filed herein by joint petitioners, for the reasons set forth herein below.

OPINION BELOW.

The basic proceeding below was a rate case before the Federal Power Commission (Commission) involving the rates of Natural. Natural and the joint petitioners each appealed the decision of the Commission, on separate grounds. Those appeals were heard by the United States Court of Appeals for the District of Columbia Circuit, Natural's appeal as Case No. 19836 and that of the joint petitioners as No. 19604. The cases were heard together and a joint opinion issued. Joint petitioners here appeal from No. 19604, in which Natural was an intervenor.

Case names, opinion numbers and dates are stated in the Petition.

QUESTION PRESENTED.

Did the Court of Appeals err in affirming the Commission's decision to require Natural to begin to use the "flow through" rate policy as of February 3, 1964, rather than as of March 1, 1961, as urged by joint petitioners? (Joint petitioners raise no question relative to the validity or propriety of use of such rate policy.)

STATEMENT OF THE CASE.

In a general rate case before the Federal Power Commission, to determine new levels of rates for the sale of natural gas by Natural, a settlement of all but a few issues was effected in 1962, with such issues left for later hearings and decision by the Commission. One of such issues related to the rate treatment of the effects upon federal income taxes of use of liberalized tax depreciation. On February 3, 1964, the Commission issued Opinion No. 417, *Alabama-Tennessee Natural Gas Company*, 31 FPC 208, affirmed 359 F.2d 318 (5th Cir.), cert. denied 385 U.S. 847 (1966), reversing its long standing policy and holding, inter alia, that the "flow through" rate policy, relative to tax use of liberalized depreciation, would be applied to Alabama-Tennessee prospectively from the date of such decision, but that the reserve accumulated by such company in accord with its long-standing practice of "normalizing" such tax expense should be retained by the company (but eliminated from its rate base). The Commission further stated that unless great differences in circumstances could be shown, such changed policy would be applied to all other natural gas pipeline companies.

In May of 1964, the Commission ordered that briefs be filed in Natural's case on the same reserved "liberalized depreciation" issue. After briefs and oral argument, the Commission held, by Opinion No. 456 issued March 18, 1965, that Natural's rates must reflect the "flow through" policy, effective as of February 3, 1964, the date upon which the Commission first adopted the "flow through" policy, in *Alabama-Tennessee*. (The other basic holding

of said opinion—the decision to apply "flow through" to Natural—has not been questioned by the Petition herein.)

On review, the United States Court of Appeals for the District of Columbia, inter alia, upheld the application of the *Alabama-Tennessee* 1964 date to Natural, but evinced "uneasiness"—not over rejection of joint petitioners' proposed 1961 date, but rather because, as Natural showed in its appeal, the Commission uniformly, except as to Natural, applied the "flow through" principle prospectively. But as to Natural, the policy was applied retroactively—by *1965* decision to the early *1964* effective date, thus requiring millions of dollars of extra refunds—even though the Commission's decision in favor of "flow through" was a complete reversal of pre-existing commission policy and decisions. Joint petitioners now seek to have this Court require the Commission to make that decision even more retroactive—by requiring refund of moneys collected back to 1961.

ARGUMENT—REASONS FOR DENYING THE WRIT.

Summary.

In summary, as discussed more fully hereinbelow, the Petition should be denied because:

1. The issue involved is of specific, not general, applicability, since it relates to only one company and the interpretation of a single, unique settlement agreement, in reference to choice of a "one-time" date.

2. The joint petitioners seek to require that the Commission be forced to make its decision against Natural become even more discriminatory than it now is, by requiring that the complete change of policy be applied to Natural over four years before that policy was found applicable to Natural. The Commission and the Court of Appeals were clearly correct in rejecting that position.

3. The Commission and the Court of Appeals were correct, as a matter of law, in holding, contrary to the claims of joint petitioners, that the settlement agreement between the parties in this case did not specify the effective date for application of any rate policy change to Natural, and that the Natural Gas Act allows the Commission discretion to avoid discrimination by making its rate case rulings effective as of a date on, *or after,* the rates involved in a rate increase case become effective.

I. The Issue Raised By Joint Petitioners Has No Significance Beyond This Case.

The basic claim of joint petitioners relates to interpretation of the terms of the settlement agreement between

the parties to Natural's rate case. It is a specific, unique document, with no general applicability. There are no standard terms in question, so that the interpretation problem has no relevance beyond this case.

The portion of the Petition which attempts to show "national importance and significance" (Section C, pages 15-16) discusses only the importance of rate case settlements, which is correct, but then jumps to the conclusion that "This administrative tool will become untenable, if not completely avoided should this decision be allowed to stand." This is an extreme and invalid conclusion, even if joint petitioners were correct in their basic position. But what is important is that their extreme conclusion could *only* be accurate by presuming the validity of the conclusion which joint petitioners are trying to prove—that the interpretation made by the Commission and the Court of Appeals, of the specific settlement agreement involved, relative to the effective date for application of the flow through policy, was clearly unreasonable and incorrect. As will be demonstrated later in this brief, joint petitioners have not shown this.

At this point, however, it is more relevant to reiterate that no topic or issue of broad significance or applicability is involved, and no injustice to the joint petitioners has been done.

II. Use Of The 1961 Date Proposed By Petitioners Would Be Even More Unjust Than The 1964 Date Used By The Commission.

As discussed earlier, the Commission refused to adopt the "flow through" policy for over ten years prior to its complete reversal of position, on February 3, 1964, in

Alabama Tennessee. The issue was reserved in Natural's rate case only because of the insistence of a petitioner, but there was no indication then that the Commission had any thought of change. Now, petitioners seek to *force* the Commission to make that reversal of policy retroactive, to March 1, 1961, almost three years *prior* to the time the Commission adopted the policy.

Further, such action would be wholly different than that taken by the Commission with regard to every other company in the industry. Specifically, the Commission has not applied the flow through policy to any company *prior* to the time it has found, in an Order *applicable to that company,* that flow through should be applied to that company. It has not, that is, except as to Natural. Whereas flow through has been applied to most companies as of dates *after* the policy was held applicable to those companies, in the case of Natural the Commission found flow through applicable in a decision regarding Natural which was issued March 18, 1965, but made the policy effective as of February 3, 1964, some thirteen months earlier. As to *no other* company has the Commission made a retroactive application.(*)

Even in the face of this discrimination against Natural, however, joint petitioners are here seeking to have this Court require the Commission to be even more discriminatory—to make its application of flow through to Natural

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(*) The Court of Appeals expressed "uneasiness" over Natural's "thorny contention" relative to this discrimination, but concluded that the "various Commission's actions" relative to the effective dates as to various companies "have been, *so to speak,* reconciled." (emphasis added) (Petition, pages 42, 44 and 45) A 1961 date as to Natural could not be "reconciled", even on a "so to speak" basis.

almost three years more retroactive, to a 1961 date which not only far precedes the finding that flow through should be applied to Natural, but which also far precedes the *first* Commission adoption of the flow through policy as to *any* company.

The inequity of joint petitioners' claims are obvious.

III. Neither The Settlement Agreement Nor The Natural Gas Act Require The Commission To Use The Retroactive 1961 Date As To Natural.

A. The Settlement Agreement Did Not Fix An Applicability Date, And Left The Commission Free To Order An Appropriate Date.

Joint petitioners have taken on the extreme burden of trying to prove that the Commission is *required,* by the terms of the Settlement Agreement, to use the retroactive March 1, 1961 date. To attempt to justify this contention, joint petitioners set forth, at the bottom of page 12 of their Petition, a passage from the Settlement Agreement. However, only a part of the passage is quoted. The *entire* relevant passage reads:

> In the event it shall be determined in these proceedings by a valid and final order of the Commission that Natural in computing its cost of service in these proceedings, must utilize the above mentioned "flow through" method of tax computation, Natural, subject to its right to seek judicial review thereof, shall make *such further refunds,* with interest at 7% per annum from the 20th day of each month in which each excess payment was collected, to the date Natural refunds such excess payments, *as shall result from the reduction,* if any, in the level of any of the rates contained in its FPC Rate Schedules *that may be required by the Commission at the time of such order*; . . . (emphasis added) (Petition, page 67)

Thus, contrary to the misleading impression conveyed by the partial quotation in the body of joint petitioners' Petition, it is clear that the quoted passage of the settlement agreement provides that Natural shall make refunds consisting of whatever amounts *the Commission validly holds* to be an "excess payment" collected (in this case, the Commission held that such amount was the difference between rate levels under "normalization" and under "flow through", *for the period February 3, 1964 forward*). Assuming, *arguendo,* that "flow through" is a valid policy and that the Commission can make its order retroactive at all, the point here is that the *Settlement Agreement* left it for the Commission to decide whether to go back to March 1, 1961. It did not *require any* retroactivity, much less back to 1961.

The above Settlement Agreement language refers to Natural making "such further refunds * * * as shall result from the reduction, *if any,* in the level of any of the rates * * *," and the here emphasized "if any" language shows clearly that the possibility of *no* refunds (and/or no rate reductions)—which would mean no retroactivity—was left open; but in the face of this, joint petitioners claim that extreme retroactivity is required.

It is also significant that the *Settlement Agreement* language speaks of Natural being required to make "any refunds and/or rate reductions" by a particular distribution method and of Natural's obligations to make "such further refunds," with interest, "as shall result from the reduction, *if any*" in Natural's rates "that may be required by the Commission at the time of such order" requiring "flow through". The significance of the rate reduction-refund language, of course, is that if "flow

through" were ordered to be effective only prospectively from or after the date of the Commission's order, then only a reduction in Natural's rates would be ordered. On the other hand, if the order were made retroactive, as the Commission has attempted to do, then refunds, too, would be ordered. The language of the Settlement Agreement shows that *both* possibilities were contemplated, so that the Commission was left free, *by the Settlement Agreement,* to choose either a prospective or retroactive date.(*)

Further, the fact that the language of the Settlement Agreement provides that the "refunds," and the "reduction" in the "level of rates," which may be made if "flow through" was ordered and upheld, were to be those "that *may* be required by the Commission at the time of such order" shows, again, that Commission discretion is provided for. And this is consistent with the fact that the "question of whether Natural, in computing its cost of service for rate purposes," should use "normalization" or "flow through" was left for "adjudication by the Commission in these proceedings." (First sentence, Section IV (2), Settlement Agreement; Petition, page 66). An *adjudication* posits that all facets of the issue are to be decided—not, as petitioners claim, that the important issue of the length of the period for calculation of re-

(*) The Petition also refers to a letter from Natural's counsel (Petition, page 11). That letter, too, expresses the understanding of all parties that refunds (retroactive application) are a *possibility* under the Settlement Agreement, if the Commission did, and could, so order (Petition, page 55). But that is far different from saying, as do Petitioners, that the Commission *must* order refunds, particularly back to 1961. (See the Commission holding on this point, Petition, pages 72-73.)

funds, "if any," was predetermined, even though *all other* aspects of the issue were left for Commission decision.

Finally, the last sentence of Section IV (2) of the Settlement Agreement again shows that only a *possibility*, not a *certainty*, of refunds (retroactive application) was provided. It reads:

> Any refunds and/or rate reductions made by reason of this Section IV (2) shall be made as described in the last paragraph of Section IV (1) above. (Petition, page 67)

The reference to "any refunds *and/or* rate reductions" clearly contemplates that refunds *or* future rate reductions *or* both, *or*, as shown by the word "any," *neither*, could be ordered. It shows definitely that refunds do not automatically follow, even from a Commission determination that Natural must start to use "flow through," much less refunds back to 1961.

Thus, the Commission was clearly correct when it held, in Opinion No. 456, relative to the claims of the City of Chicago:

> It is entirely clear to us that the agreement was drafted with the possibility of refunds in mind. Thus it is provided that "In the event it shall be determined" that Natural must use "flow-through", it "shall make such further refunds . . . as shall result from the reduction, if any, in the level of any of the rates contained in its FPC Rate Schedules that may be requested by the Commission . . ." However, it is also clear that the refund is made contingent on the action we might take on the question of liberalized depreciation and there is no language in the settlement which can fairly be interpreted as requiring us to order refunds retroactive to the date the rate increase was put into effect by Natural. (Petition, page 72).

The Commission also correctly held, referring to its earlier decision:

> Opinion No. 367 approving the settlement does not lead to a different result. The relevant language reads as follows (28 FPC at p. 733):
>
> > The second issue is whether Natural should "normalize" its tax expense to eliminate the effect of Int. Rev. Code §167, relating to accelerated depreciation, or should compute its tax expense on the basis of taxes actually paid during the test year (1960). The settlement provides further that pending our decision on these issues, Natural shall collect revenues subject to refund based upon a 52% tax rate and "normalized" depreciation.
>
> This language, like that in the settlement agreement, does not require a refund as of any particular date, although it does contemplate a refund if that should be required by our determination. (Petition, page 73).

The Court of Appeals for the District of Columbia agreed, stating in reference to the contentions of the Petitioners:

> But we do not read the Settlement Agreement as they do. Unlike the issue of rate base reduction previously discussed, the Settlement Agreement clearly does call on the Commission to issue a decision on the issue of Federal tax expense allowances. The parties said in effect: On this issue we cannot work out a settlement, and we leave it to the Commission to decide. The parties may well have assumed that any flow-through decision would be retroactive to 1961, they may have wholly failed to anticipate the possibility that the decision would be prospective, but they did not purport to fetter the Commission's discretion to make its decision prospective. In reaching

its decision on the issues referred to it, the Commission was free to announce and apply the principles it deemed proper under the Natural Gas Act just as if it were disposing of a proceeding in which there had been no settlement. We have already upheld, as in accordance with its discretion under the Natural Gas Act, the Commission's decision, not only to provide for a "flow through" policy, but also to prescribe a 1964 effective date therefor. We do not think the Settlement prohibited application of that approach to Natural. (Petition, page 46).

The above discussion is sufficient to demonstrate that the settlement agreement in question does not require the Commission to apply "flow through" retroactively, to March 1, 1961 or any other date.

B. The Natural Gas Act Does Not Require Application Of A New Policy Retroactively.

It is clear that under the Natural Gas Act, the basic general limitation upon the Commission as to effective dates is that when a natural gas company files a notice of a change in its rates, as Natural did in 1960 to begin the rate case proceeding below, the Commission can make its decision therein effective no *earlier* than the date on which the company began to collect the new changed rates. In the proceedings below, that date was March 1, 1961. The City of Chicago takes the position that such *earliest possible* date is *the date* on which the Commission was *required* to make its "flow through" decision effective. This is a clearly incorrect position, which was rejected by the Commission and the Court of Appeals below. Joint petitioners argue that the Natural Gas Act requires that Natural must make refunds back to March 1, 1961. Their claim is based, it seems, wholly on language

from *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*, 350 U.S. 332, 341 (1956), where this Court held that one of the "*powers*" of the Commission is to make its rate case "order retroactive, by means of the refund procedure, to the date the change became effective" after suspension under Section 4(e) of the Act. It is significant that this Court said "powers," not "duties".

Natural agrees, of course, that Section 4(e) of the Natural Gas Act confers that *power* of retroactivity. But joint petitioners argue that it is not only a *power*, but a mandatory *duty*, in all cases. This is in error and the Court of Appeals so held. (Petition, page 39) First, in *United*, this Court recognized that the use of the permissive word "may" in Section 4(e) of the Natural Gas Act means that retroactive orders, by means of a refund, are permissive, but not mandatory. The statute provides:

> Where increased rates or charges are thus made effective, * * * the Commission *may*, by order, require the natural-gas company to furnish a bond, to be approved by the Commission, to refund any amounts ordered by the Commission, * * * and, upon completion of the hearing and decision, to order such natural-gas company to refund, with interest, the portion of such increased rates or charges by its decision found not justified. (52 Stat. 882; 15 U.S.C. § 717c(e), emphasis added.) (Petition, page 51).

Note that the Commission "*may*" order a bond and "*may*" order refunds, and any refunds are to be of such amounts as may be "ordered by the Commission," because such amounts are to be the "*portion*" (not necessarily all) of "such increased rates or charges by its decision found not justified." The Commission in these proceedings found that "flow through" (and revenues

associated) did not become unjustified until February 3, 1964.

The *United* case itself does not support Chicago's arguments, since it makes no holding about refunds, back to the effective date of rate increases or otherwise. Nor does any other case hold that refunds to such retroactive date are *mandatory* under the Natural Gas Act, and joint petitioners have cited none. The courts in other cases also consistently use the permissive word "may" when ruling with regard to Section 4 of the Natural Gas Act. See e.g., *Wisconsin* v. *F.P.C.*, 303 F.2d 380, 382, 386 (D.C. Cir. 1961), affirmed 373 U.S. 294 (1963); *State Corp. Commission of Kansas* v. *F.P.C.*, 215 F.2d 176, 183 (8th Cir. 1954); and *United Gas Improvement Co.* v. *Callery Properties, Inc.*, 382 U.S. 223, at 229, n. 4 (1965). See particularly *Public Service Commission of New York* v. *F.P.C.*, 329 F.2d 242, 248-250 (1964), cert. denied sub nom., *Prado Oil & Gas Co.* v. *F.P.C.*, 377 U.S. 963 (1964), where the Court of Appeals held that the Commission had power to order refunds, but that this power is not mandatory but rather is to be governed by "the standard of equity."

It is thus clear that the Natural Gas Act, like the 1962 Settlement Agreement, grants *power* to the Commission to order refunds—even to as far back as March 1, 1961—but does *not require* the Commission to do so. The Commission chose to exercise this power by requiring refunds to the retroactive February 3, 1964 date, but not to March 1, 1961. The Commission did this to be consistent with its *Alabama-Tennessee* decision, where the Commission, without objection, did not order any refunds, but rather made its decision prospective from the date of decision and the Commission has made no other decision on this issue retro-

active. Thus, the claims of petitioners, that extreme retroactivity is required, are in error.(*)

CONCLUSION.

For the reasons specified hereinabove—including the fact that the opinion of the Court of Appeals for the District of Columbia, with regard to the points raised in the Petition herein, is clearly correct and that there is no conflict of circuits to be resolved—Natural Gas Pipeline Company of America respectfully requests that the Petition for Writ of Certiorari of joint petitioners herein be denied.

Respectfully submitted,

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(*) Petitioners also exhibit inconsistency in their own positions, since the Public Service Commission of Wisconsin, in regulating Wisconsin utilities, negates the "flow through" policy by an additional depreciation allowance. Yet here, they not only urge a complete flow through policy (un-negated), but also ask that it be applied *retroactively*. Similarly, the City of Chicago does not urge the flow through policy for Illinois companies, before the Illinois Commerce Commission, but urges such policy, retroactively, upon Natural.

In the Supreme Court of the United States

OCTOBER TERM, 1967

PUBLIC SERVICE COMMISSION OF THE STATE OF WISCONSIN AND CITY OF CHICAGO, A MUNICIPAL CORPORATION OF THE STATE OF ILLINOIS, PETITIONERS

v.

FEDERAL POWER COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE FEDERAL POWER COMMISSION IN OPPOSITION

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. A, 19–46) is not yet reported. The opinions of the Federal Power Commission (Pet. App. G, 68–83; App. H, 84–91) are reported at 33 F.P.C. 574, 1277.

JURISDICTION

The judgment of the court of appeals was entered September 8, 1967. By order entered October 31, 1967 (Pet. App. B, 47), the court of appeals granted petitioners' motion for stay of transmittal of the opinion and certified copy of its judgment in case No. 19604 for 30 days and denied the petition of Natural Gas

288-663—68

Pipeline Company of America for rehearing in case No. 19836. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1) and Section 19(b) of the Natural Gas Act, 15 U.S.C. 717r(b).

QUESTION PRESENTED

Whether Section 4(e) of the Natural Gas Act, or a Commission-approved settlement agreement among the parties, required the Federal Power Commission to order the Natural Gas Pipeline Company of America to make refunds as a result of a change in the Commission's policy—regarding the computation of the allowance of federal income taxes in the Company's rates—effective as of the date when Natural began to collect, subject to refund, the rates based on the pre-existing policy, rather than as of the later date on which the policy change was first announced to the industry.

STATUTE INVOLVED

Section 4(e) of the Natural Gas Act, June 21, 1938, c. 556, 52 Stat. 882, 15 U.S.C. (1958 ed.) 717c(e), is set forth in the petition, App. C, 50–52.

STATEMENT

On August 29, 1960, Natural Gas Pipeline Company of America, pursuant to Section 4(d) of the Natural Gas Act, filed with the Federal Power Commission a schedule of increased rates.[1] The Commission sus-

[1] The rate increases were filed by Natural and by Peoples Gulf Coast Natural Gas Pipeline Company. The two companies were combined on September 29, 1960, and will be referred to herein solely as "Natural."

pended these rates under Section 4(e) of the Act for the maximum statutory period of five months. Subsequently, on March 1, 1961, Natural put the rates into effect, subject to its obligation to refund such revenues derived from the new rates as the Commission might subsequently find unjustified.

Before the hearing examiner issued his decision, Natural entered into a settlement agreement with other parties, including petitioners (J.A. 291–305), which the Commission approved (Pet. App. E, 63). This agreement resolved most pending questions. It reduced the proposed increases in rates by about half and Natural undertook to refund the excess collected.

The settlement reserved for future Commission determination, *inter alia,* an issue regarding the federal tax allowance to be included in Natural's cost of service. Natural agreed, if this issue should be decided against it, to make further refunds, with interest, of "such excess payments, as shall result from the reduction, if any, in the level of any of the rates contained in its FPC Rate Schedules that may be required by the Commission at the time of such order * * *" (Pet. App. F, 67).

The tax issue grew from Natural's practice of reducing its tax liability by taking liberalized depreciation, but, under the then effective Commission policy, including in its costs for rate purposes the higher taxes that would have resulted from taking straight-line depreciation, and setting aside in a deferred tax reserve the difference between this "normalized" tax and the actual tax paid. Chicago contended that the Commission should change its policy and require

pipeline companies to "flow through" the tax advantages of liberalized depreciation by including in costs only the taxes actually paid.

The Commission had indicated, prior to the settlement agreement, that it was reconsidering the tax question.[2] On June 1, 1962, it ordered oral argument on that issue in *Alabama-Tennessee Natural Gas Co.* and invited *amicus* participation by anyone having an interest in the problem. 27 F.P.C. 1063. On February 3, 1964, the Commission announced as its new general policy that "flow-through" was the proper method of computing federal income tax allowances for rate making purposes. *Alabama-Tennessee Natural Gas Co.*, 31 F.P.C. 208. The same issue had been reserved in orders prescribing future rates for other companies; the Commission said that as to them the *Alabama-Tennessee* decision would constitute a proposed decision. 31 F.P.C. at 209.

Thereafter Chicago moved the Commission to decide the issue as to Natural. Natural, in its answer (J.A. 366–377), offered to accept the Commission's decision in *Alabama-Tennessee* if it were judicially affirmed,[3] provided that refunds on that account would be made only for a period beginning October 1, 1965, and only if Natural had not before that date elected to abandon

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[2] See *Idaho Power Company*, 27 FPC 349, 352; *Minnesota Power & Light Company*, 27 FPC 354, 357; *Southern California Edison Company*, 27 FPC 360, 363; *New England Power Company*, 27 FPC 404, 406; and *California Electric Power Company*, 27 FPC 658, 662.

[3] The Fifth Circuit affirmed the Commission on March 25, 166 (359 F. 2d 318), and certiorari was denied on October 10, 1966 (385 U.S. 847).

use of liberalized depreciation (J.A. 373–375). Chicago and the other petitioner here, the Wisconsin Public Service Commission, urged rejection of Natural's proposal on the ground, *inter alia,* that, under the settlement agreement, the refunds should date back to March 1961.

The Commission, in Opinion No. 456 (Pet. App. G, 68–83), held that the principles of *Alabama-Tennessee* were applicable to Natural, and ordered Natural to make refunds for the period beginning February 3, 1964, the date of the *Alabama-Tennessee* decision (Pet. App. G, 77). On rehearing the Commission denied both Natural's claim that October 1, 1965 (J.A. 433–434), and petitioners' claim that March 1, 1961 (J.A. 411–412), should begin the refund period (Pet. App. H, 90). The Court of Appeals for the District of Columbia Circuit unanimously affirmed on this issue (Pet. App. A, 38–46).[4]

ARGUMENT

The petition presents no issue of general import. The narrow question of the interpretation of a particular settlement agreement such as the one involved here does not warrant plenary review by this Court. Nor is there merit to the contention that the Commission has no discretion to order refunds from a date

[4] The court affirmed the Commission's decision to reflect only actual federal income taxes in Natural's rates (Pet. App. A, 21–33). It reversed, however, the Commission's decision requiring the reduction of Natural's rate base by the accumulated deferred tax reserve on the ground that that issue was not reserved for future determination by the Commission-approved settlement agreement. The court's decision in these respects is not at issue here.

later than the effective date of rates collected subject to refund.

1. "Normalization" was the lawful and proper method of computing federal income taxes for rate-making purposes until the Commission changed its policy on February 3, 1964. See, *e.g.*, *El Paso Natural Gas Co.* v. *Federal Power Commission*, 281 F. 2d 567, 573–574 (C.A. 5), certiorari denied, *sub nom. California* v. *Federal Power Commission*, 366 U.S. 912. So long as the old policy remained in effect rates based thereon were lawful rates. The "flow-through" policy represented a significant change in the policies that determine rates.

Section 4(e) of the Act provides that the Commission "may" order the refund of "the portion of such increased rates or charges by its decision found not justified." There is no basis for reading into this permissive language, as petitioners would, a command to apply the same rate throughout the refund period. The only proper question is whether the Commission acted reasonably in selecting an intermediate date for the start of refunds resulting from this general change of policy. Here the Commission's decision was to make a fundamental change in policy prospective from the date it was first announced. Surely it was not unreasonable to attempt in this way to be as even-handed as the circumstances allowed in the treatment accorded the various members of a single industry.

2. As the court below and the Commission found, nothing in the agreement committed Natural to make, or the Commission to order, refunds back to March 1, 1961, if the Commission determined that flow-through

was the appropriate treatment of the use of liberalized depreciation (Pet. App. G, 74). The agreement merely provided, and did so expressly, that Natural would make such further refunds of the increased rates put into effect on March 1, 1961, as would result from a reduction in the level of rates required by the Commission in its order deciding the "flow through" question (Pet. App. F, 67). This left it to the Commission to decide that issue and the date as of which, as a matter of regulatory policy, flow-through, if that should be required, should be made applicable to Natural. As the court of appeals correctly found, the agreement of the parties "did not purport to fetter the Commission's discretion to make its decision prospective" (Pet. App. A, 45–46).

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1967

No. 893

PUBLIC SERVICE COMMISSION OF THE STATE OF WISCONSIN,

and

CITY OF CHICAGO, A MUNICIPAL CORPORATION IN THE STATE OF ILLINOIS, *Joint Petitioners,*

v.

FEDERAL POWER COMMISSION, *Respondent.*

BRIEF AMICI CURIAE ON BEHALF OF VILLAGE OF BETHANY, ILLINOIS; CITY OF CORNING, IOWA; CITY OF PINCKNEYVILLE, ILLINOIS; AND CITY OF SPEARVILLE, KANSAS; IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

Pursuant to Rule 42(4) of the Revised Rules of the Supreme Court of the United States, the Village of Bethany, Illinois; the City of Corning, Iowa; the City of Pinckneyville, Illinois; and the City of Spearville, Kansas, all political subdivisions of their respective

states, submit this Brief Amici Curiae in support of the Petition for a Writ of Certiorari filed by the Public Service Commission of the State of Wisconsin and the City of Chicago, a Municipal Corporation of the State of Illinois (Joint Petitioners) seeking review and ultimate reversal of an adverse decision by the United States Court of Appeals for the District of Columbia in *City of Chicago* v. *FPC,* F. 2d , slip opinion, Nos. 19604 and 19836 (D.C. Cir. 1967) (Pet. App. 19-46).

INTEREST OF AMICI CURIAE

The villages, towns and cities located in Illinois, Iowa, and Kansas joining in this Amici Brief to the Court each own and operate a gas distribution system within their respective communities serving the people, schools, municipal buildings, churches, and businesses located therein. The sole source of natural gas for their distribution systems is from the respondent, Natural Gas Pipeline Company of America (Natural). The wholesale rates charged by Natural for gas delivered at the city gates are paid directly by the amici and dictate to a substantial degree the retail price to the individual gas consumers served by their systems. While the amici are but small municipalities their proportionate share of the approximate $30 million refund at stake in the pending petition for certiorari represents, to them, a substantial sum for their respective communities.

The amici, although political subdivisions of their respective states, have no regulatory powers over the wholesale rates charged to them by Natural, an interstate pipeline company. Congress enacted the Natural Gas Act (Act) with the "primary aim . . . to protect

consumers against exploitation at the hands of natural gas companies" [1] and charged the Federal Power Commission (Commission) with the administration of the Act. By setting aside the Commission-approved Settlement Agreement whereby Natural agreed to refund to its consumers any excessive rates collected by the Company since March 1, 1961 relating to the liberalized depreciation issue, the Commission and court below inverted the purpose of Congress contrary to the scope of its powers under the Act and existing precedents to the prejudice and detriment of the amici.

REASONS FOR GRANTING THE WRIT

I. Congress Has Not Delegated to the Commission the Authority It Now Asserts Under Section 4(e) of the Act To Exercise Its Discretion To Alter the Explicit Refund Provisions of Said Section of the Act, and the Supreme Court Should Review This Novel and Unprecedented Interpretation of the Natural Gas Act

The Commission contends in the present case (Pet. App. 75), and the court below affirmed (Pet App. 41),[2] that the Commission has "equitable power" arising out of Section 4(e) of the Act to set refund dates according to its own conceptions of fairness. Thus in the instant case, it has said Natural's customers may collect refunds for illegal rates only from February 3, 1964, rather than March 1, 1961, the effective date of said illegal rates.

The most definitive statement regarding the effect of Section 4(e) is found in the oft-cited case of *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*, 350

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[1] *FPC* v. *Hope Natural Gas Co.*, 320 U.S. 591, 610 (1944).

[2] *Natural Gas Pipeline Co. of America*, 33 FPC 574, 1277 (1965), *aff'd, City of Chicago* v. *FPC*, — F. 2d —, Nos. 19604 and 19836 (D.C. Cir. 1967) (Pet. App. 68, 19).

U.S. 332, 341 (1956), in which a natural gas company unsuccessfully attempted to unilaterally alter a rate settlement. The Court stated that Section 4(e) empowers the Commission to maintain the status quo pending review of new rates by suspending their operation for a limited period and "thereafter to make its order retroactive, by means of the refund procedure, *to the date the change became effective.*" (Emphasis added.) See *FPC* v. *Hunt,* 376 U.S. 515, 522 (1964); *Phillips Petroleum Co.* v. *FPC,* 349 F. 2d 535, 539 (10th Cir. 1965); *Shell Oil Co.* v. *FPC,* 334 F. 2d 1008 (3rd Cir. 1964). It has always been axiomatic under the Act (Section 4(e)) that refunds due and owing as the result of the imposition of unlawfully inflated rates begin to run from the *effective date* of the increased rates. *E.g., FPC* v. *Tennessee Gas Transmission Co.,* 371 U.S. 145, 152 (1962); *Id.* So far as the intent of Section 4(e), the protective provision in question speaks for itself; it was obviously inserted to guard the gas consuming public against the imposition of unlawfully inflated rates, consistent with the overall intent of Congress, as noted above, to protect the consumers from exploitation at the hands of pipeline companies. *E.g., FPC* v. *Hope Natural Gas Co., supra* at 610. Nothing in the Act or the cases suggests the "equitable" powers now claimed for the Commission to use Section 4(e) not to protect consumers but to deprive them of refunds otherwise due. As the Supreme Court more recently noted, "the purpose of the Act is 'to afford consumers a complete, permanent and effective bond of protection from excessive rates and charges. . . .'" *FPC* v. *Tennessee Gas Transmission Co., supra* at 154. *FPC* v. *Interstate Natural Gas Co.,* 336 U.S. 577, 581 (1949) (to the same effect). In addition, whenever the financial interest of the consumer and the pipeline company collide, the Supreme Court

has inevitably come down unhesitatingly on the side of the consumer as required by the Natural Gas Act. *E.g., Id.* at 153 (even where gas company might suffer some unrecoverable losses, "[s]uch situations are entirely consistent with the policy of the Act and . . . occur with frequence.")

In summary, we are aware of no case extant[3]—nor have the Commission or lower court cited any—which holds that the Commission has the power to rewrite the refund provisions of Section 4(e) of the Act to conform with its desires in any given case. This court, however, must be wary of general statements such as the following which, cited out of context, can be misleading: "In *Federal Power Commission* v. *Tennessee Gas Transmission Company* [*supra*] . . . , the Supreme Court stressed the flexibility of the Commission's power over refunds." *Texas Eastern Transmission Corp.* v. *FPC,* 357 F. 2d 232, 240 (5th Cir. 1966). In the cited (*Tennessee*) case, the court was upholding the use by the Commission of interim order proceedings resulting in the *expedited* return of refunds back to effective date of the illegal rate increase; in so doing the court was commending the Commission in its use of proper administrative tools to protect consumers against exploitation and assure just and reasonable rates. *FPC* v. *Tennessee Gas Transmission Co., supra,* at 154. In the *Texas Eastern* case from which the above quote was taken, the circumstances are equally telling. There, the court was concerned with the Commission's power to see that refunds (collected from producers from *effec-*

[3] We are, of course, referring to cases antedating the instant one; that the Commission may consider the instant one as precedent for similar subsequent action is of no consequence. Such a see-saw argument defies judicial logic.

tive date of overcharges) were ultimately returned to the gas consumers and did not stop in the treasuries of the pipeline companies who were overcharged in the first instance. Though the court reached no decision on the issue of the power of the Commission in this respect, it is important to notice that as in the *Tennessee* case, the court was only concerned to insure that the gas consumer received his *full* due (i.e., overcharges since effective date of illegal rates) consistent with the clear intent of the Act and Section 4(e) of said Act.

In review, it is apparent that the Commission's attempt to allow Natural to retain admitted overcharges from March 1, 1961, the effective date of the unlawful rates, to February 3, 1964, not only usurps power denied it under § 4(e) of the Act but even worse, amounts to an illegal exercise of discretion *at the expense of the gas consumer,* the "intended beneficiary" of the Act,[4] directly contrary to the express desires of Congress.

II. The Commission's Attempt To Override a Binding Settlement Agreement as Well as Section 4(e) of the Act Is Contrary to the Established Statutory and Case Law and Provides an Important Precedent Detrimental to the Administration of the Natural Gas Act for the Protection of Consumers

On October 25, 1962, the Commission approved a Settlement Agreement between Natural, it customers, the City of Chicago, the Wisconsin Public Service Commission, and the Staff which specifically reserved the contested issue of the proper treatment of liberalized depreciation for future consideration and which also provided for refunds dating from the effective date (March 1, 1961) of the rate increase in question should

[4] *FPC* v. *Interstate Natural Gas Co., supra* at 581.

the reserved issue be decided adversely to Natural.[5] *Re Natural Gas Pipeline Co. of America,* 28 FPC 731 (1962) (Pet. App. 58). However, despite the Settlement Agreement, the Commission, three years after approving the Agreement, proceeded to ignore the admittedly "binding contract" (Pet. App. 70) because, in its own words, "[w]e think the most equitable resolution of this matter is to put Natural on a par with *Alabama-Tennessee.*" (Pet. App. 75.) In short, due to the pure happenstance that *Alabama-Tennessee*[6] decided the issue of the proper treatment of accelerated depreciation as of February 3, 1964, refunds due and owing to Natural's customers resulting from admittedly excessive rates effective since March 1, 1961, *at which time* the accelerated depreciation issue was specifically reserved for future treatment, must be forfeited. This defies common sense as well as the plain meaning of the Commission-approved Settlement Agreement. As dissenting Commissioner Black so aptly phrased it:

> "It is not at all uncommon in settlement proceedings or, for that matter, in fully adjudicated cases, for the parties or the Commission to reserve an issue for subsequent determination. When the severed issue is decided, *unless specific provision is made to the contrary,* it will relate back in time,

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[5] To avoid any inference, much less argument, that the decisions of the Commission and of the affirming Court were "interpretive" in their outlook, Part III, infra, has been added to show not only the clear meaning of the Settlement Agreement but in addition the admitted indifference of the Commission and of the Court to its content.

[6] *Alabama-Tennessee Natural Gas Co.,* 31 F.P.C. 208 (1964), *aff'd, Alabama-Tennessee Natural Gas Co.* v. *FPC,* 359 F. 2d 318 (5th Cir. 1966), *cert. denied,* 385 U.S. 847 (1966).

> utilizing the same test period, and fit into the agreement or the decision of the Commission just as if it had been decided along with the other issues." * (Pet. App. 80.) (Emphasis added.)
>
> * Footnote omitted.

But even more fatal to the Commission's so-called "equitable" determination than its illogicality is the complete absence of any mention, or even inference, in the refund Section (4(e)) of the Act of any discretionary power lodged in the Commission to alter a Settlement Agreement reaffirming the intent of the parties to provide for refunds from the effective date of rate increase should the contested portion of the rates be declared unlawful. *Phillips Petroleum Co.* v. *FPC*, 349 F. 2d 535 (10th Cir. 1965).

The decision of the court below held unequivocably that the Commission could ignore the terms of a Settlement Agreement (and thus necessarily Section 4(e)), as illustrated by the following conclusion:

> "The parties may well have assumed that any flow-through decision would be retroactive to 1961, they may have wholly failed to anticipate the possibility that the decision would be prospective, but they did not purport to fetter the Commission's discretion to make its decision prospective. In reaching its decision on the issues referred to it, the Commission was free to announce and apply the principles it deemed proper under the Natural Gas Act *just as if it were disposing of a proceeding in which there had been no settlement.*" (Pet. App. 46.) (Emphasis added.)

Not only is this holding clearly wrong in light of the undisputed meaning and interpretation given to Section 4(e) (as illustrated in Part I, *supra*) by Congress,

the Courts, and heretofore the Commission, but in addition, Section 4(e) aside, it appears directly contrary to a holding by the United States Court of Appeals for the Tenth Circuit as follows:

> "The refund was required by *contract* and no party contends otherwise. Since it was so required, El Paso could have commenced *legal* proceedings to enforce its rights and *no regulatory action* was required to permit it to do so." *Phillips Petroleum Co.* v. *FPC, supra* at 540 (Emphasis added).

The Court went on to conclude that where *separate refund agreement* provisions are present "the obligation to refund exists *independently of the regulatory processes.*" *Id.* (Emphasis added).

The reasoning of the court below is equally unconvincing. Unable to find any concrete support, either within the Natural Gas Act or related cases, for the Commission's exercise of "equitable powers" under the instant circumstances, the court indulged in imprecise and unrelated generalities concerning the "[i]nstructive analogy" to be found within the "legislative and judicial branches." (Pet. App. 39.) This discussion led the court to conclude that though an administrative body does not have equity powers of a judicial nature, "it may have recourse to equitable conceptions in striving for the reasonableness that broadly identifies the ambit of sound discretion." (Pet. App. 41.) Generalities of this nature, however, lend nothing to a meaningful interpretation of the Natural Gas Act, much less to the Commission's delegated authority within said Act. Further, and more important, certainly the Commission should have no powers to set aside settlement agreements expressly protecting consumers; if the Commission is to have such "equi-

table'' powers it is for the Congress, not the courts, to say so.

There is a great importance to a resolution of the question of the propriety of the lower court's holding by this Court. Settlement agreements have been a useful means in recent years of expediting the handling of multifaceted, time-consuming, and, to the small consumer, expensive rate proceedings. The value of settlement agreements to the consumer, as well as to the industry, has been recognized on numerous occasions. *E.g., Texas Eastern Transmission Corp.* v. *FPC,* 306 F. 2d 345, 347 (5th Cir. 1962). But what party will dare to enter, much less rely upon, a Commission-approved settlement agreement involving significant sums of money when there is no degree of certainty that in years to come the Commission will feel bound by its terms?

These adverse effects are clear in the present case. The parties in entering the agreement to settle the pending rate case with Natural clearly did so as the Commission and court apparently agree in the belief that they would be entitled to refunds should that portion of the increase then to be collected relating to the liberalized depreciation issue be ruled illegal. The subsequent ruling by the court below, that the Commission may override the Settlement Agreement to deprive the consumers of $30 million in admittedly excess rates collected by Natural, obviously undercuts the entire basis upon which the consumers entered the agreement. As Commissioner Black aptly stated in his dissent:

> "Here we have approved one settlement on the basis of which the parties discontinued their litigation. We are now, three years later, imposing on them an entirely different 'settlement.' In my

opinion the parties clearly would not have consummated their agreement had they known what would happen to it at the hands of the Federal Power Commission." (Pet. App. 82.)

III. The Settlement Agreement So Studiously Avoided by the Commission and Reviewing Court Clearly Contemplated Refunds Dating From March 1, 1961, the Effective Date of Natural's Rate Increase

Though as has been evident from the above, and will be illustrated further below, both the Commission and the Court of Appeals rendered decisions independent of the Settlement Agreement, a summary review of the Settlement Agreement—its terms and the environment in which it was negotiated—will be presented to guard against any contention seeking to avoid review by urging that it and the reviewing court's decisions were "interpretive."

As is evident from the above discussion of the Act (Section 4(e)) and of cases connnected therewith (see Parts I and II, *supra*), parties providing for refund provisions in rate settlements always contemplate refunds dating from the effective date of the illegal rates unless clearly specified to the contrary. Thus, it is clear what Natural's eminent counsel meant when he stated in a cover letter attached to the subject Settlement Agreement that "Natural also agrees to go to trial before the FPC on two issues and if it loses on either, to make *additional refunds and rate reductions* (over and above the unconditional ones mentioned above)." (Pet. App. 55.) (Emphasis already supplied.) It is clear that the "additional refunds," should they be required, were to be treated on a par with the "unconditional ones" which, the preceding paragraph makes clear, were to date from the effective date

of the rate increase, March 1, 1961.[7] *Id.*. The pertinent parts of the Settlement Agreement itself, though mentioning no specific date per se, are equally clear as to the intent of the parties:

> "In the event it shall be determined in these proceedings by a valid and final order of the Commission that Natural in computing its cost of service in these proceedings, must utilize the above mentioned "flow through" method of tax computation, Natural, subject to its right to seek judicial review thereof, *shall make such further refunds with interest at 7% per annum from the 20th day of each month in which each excess payment was collected,* to the date Natural refunds such excess payments, as shall result from the reduction, if any, in the level of any of the rates contained in its FPC Rate Schedules that may be required by the Commission at the time of such order." (Pet. App. 67.) (Emphasis already supplied.)

In approving the Settlement Agreement, the Commission noted that "pending our decision on these [reserved] issues, *Natural shall collect revenues subject to refund. . . .*" *Re Natural Gas Pipeline Co. of America,* Opinion No. 367, 28 FPC 731, 732 (1962) (Pet. App. 59) (emphasis added). This short proviso makes it abundantly clear that all revenues collected by Natural after March 1, 1961, were subject to refund. There is no sign or indication whatever in any of these documents that the parties contemplated an alternative date from which to collect refunds.

Apparently realizing that the above documents speak clearly for themselves, the Commission and the affirm-

[7] Re Natural Gas Pipeline Co. of America, Opinion No. 367, 28 FPC 731 (1962) (Pet. App. 59) (Ordering paragraph (D) specified March 1, 1961 as retroactive date for unconditional refunds).

ing court completely dodged the issue as to the internal meaning of the agreement.

In Opinion 456,[8] the disputed decision affirmed below, the Commission disposed of the above-recited documents in a most novel fashion. Though admitting that "the settlement represents a binding contract" and that "it is entirely clear . . . that the agreement was drafted with the possibility of refunds in mind," the Commission attempted to free itself from the effect of the admittedly "binding contract" by concluding that there was "no language in the settlement which can fairly be interpreted as *requiring* us to order refunds retroactive to the date the rate increase was put into effect by Natural." (Pet. App. 72.) (Emphasis added.) To paraphrase the above, the Commission justified its refusal to carry out the clear meaning of the Settlement Agreement on the grounds that the language used in it was not of such a mandatory nature that the Commission was bound by it. Not only is this refusal to even attempt to interpret a binding contract inexcusable on its face but in addition such an approach has been condemned in an analogous case. In *Texas Eastern Transmission Corp.* v. *FPC*, 306 F. 2d 345 (5th Cir. 1962), the Court was faced with the disputed interpretation of the refund provision of a settlement agreement by the Commission. The Court pointed out that the correctness of the refund order "depends on the correctness of the Commission's *interpretation* of the private contract." *Id.* at 346-47 (emphasis added). This comment should be contrasted with the instant case in which the Commision went to great lengths to

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[8] *Natural Gas Pipeline Co. of America*, 33 FPC 574 (1965) (Pet. App. 68).

avoid *any* interpretation or analysis of the contract. The *Texas Eastern* Court emphasized that "one sure way to discourge voluntary settlements is for the Commission, at the behest of one party or the other . . . to read into contracts things which are simply not expressed or not there, out of the thoroughly commendable (and understandable) feeling that unless that is done the result is not as good as it ought to have been." *Id.* at 348. In our own case, the Commission has committed the reverse sin—that of omission—by refusing to take cognizance of the clear meaning of the agreement in question. In short, the Commission has refused to recognize that a contract "should stand for what it says" (*Id.* at 348) and be given effect accordingly.

In affirming the Commission's Opinion No. 456, the reviewing court made no analysis of the internal meaning of the Settlement Agreement. It glossed over the Commission's meager reference to the contract, not even seeking to determine whether the Commission's conclusion on the subject were based on "substantial evidence." Rather, the Court made the following bald and bold statement already noted above:

> "The parties may well have assumed that any flow-through decision would be retroactive to 1961, they may have wholly failed to anticipate the possibility that the decision would be prospective, but they did not purport to fetter the Commission's discretion to make its decision prospective. In reaching its decision on the issues referred to it, the Commission was free to announce and apply the principles it deemed proper under the Natural Gas Act *just as if it were disposing of a proceeding in which there had been no settlement.* (Pet. App. 46.) (Emphasis added.)

Apparently realizing that Commission Opinion No. 456 was in direct conflict with the purport of the Settlement Agreement and could not be reconciled with its clear meaning, the Court in effect granted the Commission carte blanche to ignore the Settlement Agreement, thereby dealing the coup de grace not only to the Settlement Agreement in question but even more significantly to the future use of settlement agreements as an effective rate making tool.

The only official in a ruling capacity who bothered to take cognizance of the Settlement Agreement was Commissioner Black, who dissented from Opinion Nos. 456 and 456-A. As a result of an in-depth study of the Settlement Agreement, he concluded:

> "A matter of such vast importance and involving so many millions of dollars in refunds would hardly have been left to inference. If the parties to this case intended that application here of a legal and policy decision to be made some time in the indefinite future in another case [*Alabama-Tennessee*], would be prospective from the date that case was decided, *clearly they would have said so.*" (Pet. App. 81.) (Emphasis added.)

In summary, it can only be concluded from the above analysis that all the parties to the Settlement Agreement, including the Commission at the time of its approval order, anticipated that any and all refunds to which Natural's customers should subsequently become entitled would date from March 1, 1961. The unavoidability of this conclusion in turn accounts for the studious attempt by the Commission and by the court below to find means to disregard the terms of the Settlement Agreement.

CONCLUSION

For all the reasons stated in the above portions of this Amici Brief, the above-named municipal systems respectfully request that the Supreme Court of the United States grant the Petition for Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit filed by the Joint Petitioners.

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